

Manchester Law Office Valuation

Edward Sapp

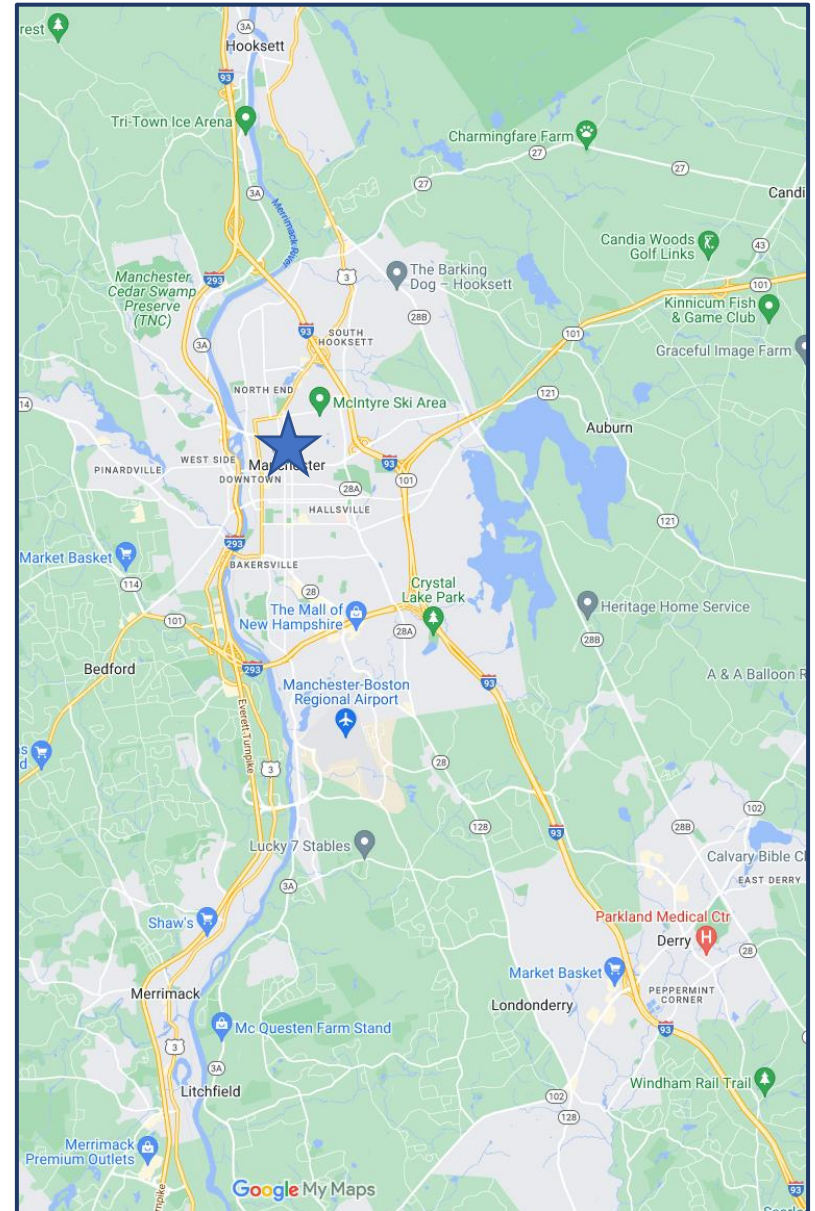
April 27th, 2023

Executive Summary

- 5 Consortium Ave (“the Property”) is a 62.9k SF Law Office Building in Manchester, NH
- The building currently has three owners (the “Seller”), two of which are retired from the group, and one is soon to retire
- The five practicing lawyers (the “Practicing Group”) and two of the Sellers (together, the “Buyer” or “Buyers”) contemplate completely buying out one of the three Sellers and partially liquidating down the other two so there would eventually be seven equal owners (14.3% each)
- The Practicing Group, Manchester Law Group, currently rents the space and represents the largest footprint at 46.9k SF, or 74.5% of the 62.9k SF building. The other tenants also represent legal uses, barring SRN Realty which occupies 752 SF or 1.2% of the building
- Manchester Law Group engaged Edward Sapp on April 25th, 2023 to determine the following:

Question	Response
Whether the \$17.0M asking price is reasonable	<ul style="list-style-type: none">• \$17.0M ask (5.0% going-in cap rate) is tight vs. 8.5% market cap rate, reflecting an inflated valuation. Further, would return 2.2% over 10-year hold period, significantly below market rate of return• \$13.2M offer would achieve client’s 5.75% hurdle rate of return• \$9.5M invested today into a relatively safe 5.75% investment account would cover rent for next 10 years
Determine potential ways to value the building in the future for when new lawyers enter/leave the Buyer group and come in and out of the LLC which owns the real estate	Short answer would be to refresh the Excel file provided in this analysis on a rolling basis. The stickiest part is always going to be to agree on a cap rate. In situations where parties need to agree, typically you each bring an appraisal and meet in the middle on cap rate and projections.
How to execute the purchase in a tax-efficient manner	Will ultimately need to contract a qualified tax advisor or accountant, tax can be a very localized beast. That said, I have outlined some high-level tax strategies on P9: 1031 Exchange, Installment Sales, Opportunity Zones.

Asset Map and Images



Transaction Summary

Owner	Ownership %			Total Basis (Purchase Price + Fees)		
	Pre-Trx	Trx	Post-Trx	Pre-Trx	Trx	Post-Trx
Seller A (Kim)	26.7%	(26.7%)	—	\$4,601,333	(\$4,601,333)	—
Seller B (Walker)	36.7%	(22.4%)	14.3%	6,326,833	(3,861,833)	2,465,000
Seller C (Davis)	36.7%	(22.4%)	14.3%	6,326,833	(3,861,833)	2,465,000
Buyer D	—	14.3%	14.3%	—	2,465,000	2,465,000
Buyer E	—	14.3%	14.3%	—	2,465,000	2,465,000
Buyer F	—	14.3%	14.3%	—	2,465,000	2,465,000
Buyer G	—	14.3%	14.3%	—	2,465,000	2,465,000
Buyer H	—	14.3%	14.3%	—	2,465,000	2,465,000
Total	100.0%	—	100.0%	\$17,255,000	—	\$17,255,000

Valuation	Entry	Exit
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Value Summary	Entry	Exit
Value	\$17,000,000	\$11,808,269
NTM NOI	855,261	1,003,703
Cap Rate	5.03%	8.50%

Transaction Costs	Entry	Exit
Transaction Cost %	1.50%	1.50%
Transaction Cost \$	\$255,000	\$177,124

Timing	
Hold Period (yrs)	10

Exit Cap Rate Comps & Exit Cap Rate for Analysis	
CBRE Boston Suburban Office Class A Value Add Cap Rate	6.75%
NAR Boston-Cambridge Office Market Cap Rate (Class A)	7.00%
SPGlobal Median Office REIT Cap Rate	9.50%
Live Exit Cap Rate (Class B Suburban)	8.50%

Sources & Uses	\$	%
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Sources		
Buyer D-H Cash	\$12,325,000	71.4%
Seller B Rolled Equity	2,465,000	14.3%
Seller C Rolled Equity	2,465,000	14.3%
Total Sources	\$17,255,000	100.0%

Uses		
Purchase Building	\$17,000,000	98.5%
Entry Costs	255,000	1.5%
Total Uses	\$17,255,000	100.0%

Returns	
UIRR	2.18%
UMoC	1.19x

Note: Model assumes building purchased at end of 2023, free-and-clear.

Valuation Sensitivity

Sensitivity Table - UIRR / MoC

		Exit Value / Exit Cap								
		\$10,565,294 9.50%	\$11,152,255 9.00%	\$11,808,269 8.50%	\$12,546,286 8.00%	\$13,382,705 7.50%	\$14,338,613 7.00%	\$15,441,583 6.50%	\$16,728,382 6.00%	\$18,249,144 5.50%
Entry Cap / Purchase Price	5.0% \$17,000,000	1.4% / 1.1x	1.8% / 1.2x	2.2% / 1.2x	2.6% / 1.2x	3.1% / 1.3x	3.6% / 1.3x	4.1% / 1.4x	4.8% / 1.5x	5.4% / 1.6x
	5.3% 16,000,000	2.2% / 1.2x	2.6% / 1.2x	3.0% / 1.3x	3.4% / 1.3x	3.9% / 1.4x	4.4% / 1.4x	4.9% / 1.5x	5.5% / 1.6x	6.2% / 1.7x
	5.7% 15,000,000	3.1% / 1.3x	3.4% / 1.3x	3.8% / 1.3x	4.3% / 1.4x	4.7% / 1.4x	5.2% / 1.5x	5.8% / 1.6x	6.4% / 1.7x	7.1% / 1.8x
	6.1% 14,000,000	4.0% / 1.4x	4.4% / 1.4x	4.8% / 1.4x	5.2% / 1.5x	5.6% / 1.6x	6.2% / 1.6x	6.7% / 1.7x	7.3% / 1.8x	8.0% / 1.9x
	6.6% 13,000,000	5.0% / 1.5x	5.4% / 1.5x	5.8% / 1.6x	6.2% / 1.6x	6.7% / 1.7x	7.2% / 1.7x	7.7% / 1.8x	8.4% / 1.9x	9.0% / 2.0x
	7.1% 12,000,000	6.1% / 1.6x	6.5% / 1.6x	6.9% / 1.7x	7.3% / 1.7x	7.8% / 1.8x	8.3% / 1.9x	8.9% / 2.0x	9.5% / 2.1x	10.2% / 2.2x
	7.8% 11,000,000	7.4% / 1.7x	7.8% / 1.8x	8.2% / 1.8x	8.6% / 1.9x	9.1% / 2.0x	9.6% / 2.1x	10.1% / 2.2x	10.7% / 2.3x	11.4% / 2.4x
	8.6% 10,000,000	8.8% / 1.9x	9.2% / 2.0x	9.6% / 2.0x	10.0% / 2.1x	10.5% / 2.2x	11.0% / 2.3x	11.5% / 2.4x	12.2% / 2.5x	12.8% / 2.6x
	9.5% 9,000,000	10.5% / 2.1x	10.8% / 2.2x	11.2% / 2.2x	11.6% / 2.3x	12.1% / 2.4x	12.6% / 2.5x	13.2% / 2.6x	13.8% / 2.8x	14.5% / 2.9x
	10.7% 8,000,000	12.4% / 2.4x	12.7% / 2.4x	13.1% / 2.5x	13.5% / 2.6x	14.0% / 2.7x	14.5% / 2.8x	15.0% / 3.0x	15.7% / 3.1x	16.3% / 3.3x

Annual Cash Flow Summary

Historical				Projected														
Cash Flow	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034			
Projection Year				—	1	2	3	4	5	6	7	8	9	10	11			
After Entry, During Hold Period?				—	1	1	1	1	1	1	1	1	1	1	—			
Is Exit Date?				—	—	—	—	—	—	—	—	—	—	1	—			
Revenue																		
Rental Income	\$1,315,947	\$1,339,551	\$1,419,310	1,419,897	1,451,587	1,480,426	1,509,786	1,539,760	1,570,307	1,601,465	1,633,247	1,665,663	1,698,728	1,732,455	1,766,856			
Turnover Vacancy	NA	NA	NA	(55,680)	(28,469)	—	—	—	—	—	—	—	—	—	—			
Total Revenue	\$1,315,947	\$1,339,551	\$1,419,310	\$1,364,217	\$1,423,118	\$1,480,426	\$1,509,786	\$1,539,760	\$1,570,307	\$1,601,465	\$1,633,247	\$1,665,663	\$1,698,728	\$1,732,455	\$1,766,856			
Growth %		1.8%	6.0%	(3.9%)	4.3%	4.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%			
Cash Expenses																		
Property Tax	(\$135,882)	(\$59,907)	(\$135,583)	(\$135,583)	(\$139,650)	(\$143,840)	(\$148,155)	(\$152,600)	(\$157,178)	(\$161,893)	(\$166,750)	(\$171,752)	(\$176,905)	(\$182,212)	(\$187,678)			
Cleaning Purchased Time	(71,368)	(48,600)	(85,207)	(85,207)	(87,763)	(90,396)	(93,108)	(95,901)	(98,778)	(101,742)	(104,794)	(107,938)	(111,176)	(114,511)	(117,946)			
Taxes	(38,600)	(48,121)	(80,690)	(80,690)	(83,111)	(85,604)	(88,172)	(90,817)	(93,542)	(96,348)	(99,239)	(102,216)	(105,282)	(108,441)	(111,694)			
Ground & Snow	(56,290)	(51,490)	(65,994)	(65,994)	(67,974)	(70,013)	(72,113)	(74,277)	(76,505)	(78,800)	(81,164)	(83,599)	(86,107)	(88,690)	(91,351)			
Repairs	(22,706)	(55,423)	(37,118)	(38,416)	(39,568)	(40,755)	(41,978)	(43,237)	(44,534)	(45,870)	(47,246)	(48,664)	(50,124)	(51,627)	(53,176)			
Insurance	(30,476)	(26,622)	(29,144)	(28,747)	(29,610)	(30,498)	(31,413)	(32,355)	(33,326)	(34,326)	(35,356)	(36,416)	(37,509)	(38,634)	(39,793)			
Water	(15,466)	(15,407)	(21,921)	(21,921)	(22,579)	(23,256)	(23,954)	(24,672)	(25,412)	(26,175)	(26,960)	(27,769)	(28,602)	(29,460)	(30,344)			
Waste Removal	(16,731)	(18,163)	(16,748)	(17,214)	(17,730)	(18,262)	(18,810)	(19,374)	(19,955)	(20,554)	(21,171)	(21,806)	(22,460)	(23,134)	(23,828)			
Legal & Accounting	(16,495)	(31,127)	(3,376)	(16,999)	(17,509)	(18,034)	(18,575)	(19,133)	(19,707)	(20,298)	(20,907)	(21,534)	(22,180)	(22,845)	(23,531)			
Electric	(14,374)	(14,913)	(14,505)	(14,597)	(15,035)	(15,486)	(15,951)	(16,429)	(16,922)	(17,430)	(17,953)	(18,491)	(19,046)	(19,617)	(20,206)			
Service Contracts	(18,822)	(10,340)	(10,000)	(13,054)	(13,446)	(13,849)	(14,264)	(14,692)	(15,133)	(15,587)	(16,055)	(16,536)	(17,032)	(17,543)	(18,070)			
Admin Purchased Time	(22,719)	(13,500)	502	(11,906)	(12,263)	(12,631)	(13,010)	(13,400)	(13,802)	(14,216)	(14,642)	(15,082)	(15,534)	(16,000)	(16,480)			
Supplies	(10,556)	(14,541)	(9,430)	(11,509)	(11,854)	(12,210)	(12,576)	(12,953)	(13,342)	(13,742)	(14,154)	(14,579)	(15,016)	(15,467)	(15,931)			
Contract Services	—	—	(25,600)	(8,533)	(8,789)	(9,053)	(9,325)	(9,604)	(9,892)	(10,189)	(10,495)	(10,810)	(11,134)	(11,468)	(11,812)			
Miscellaneous	(1,154)	(260)	(200)	(538)	(554)	(571)	(588)	(605)	(624)	(642)	(662)	(681)	(702)	(723)	(745)			
Bank Charges	(467)	(415)	(350)	(411)	(423)	(436)	(449)	(462)	(476)	(490)	(505)	(520)	(536)	(552)	(568)			
Total Expenses	(\$472,104)	(\$408,828)	(\$535,363)	(\$551,318)	(\$567,857)	(\$584,893)	(\$602,440)	(\$620,513)	(\$639,129)	(\$658,302)	(\$678,051)	(\$698,393)	(\$719,345)	(\$740,925)	(\$763,153)			
Growth %		(13.4%)	31.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%			
NOI				\$843,843	\$930,723	\$883,948	\$812,899	\$855,261	\$895,533	\$907,346	\$919,247	\$931,179	\$943,163	\$955,195	\$967,270	\$979,384	\$991,530	\$1,003,703
Growth %		10.3%	(5.0%)	(8.0%)	5.2%	4.7%	1.3%	1.3%	1.3%	1.3%	1.3%	1.3%	1.3%	1.2%	1.2%			
Margin %	64.1%	69.5%	62.3%	59.6%	60.1%	60.5%	60.1%	59.7%	59.3%	58.9%	58.5%	58.1%	57.7%	57.2%	56.8%			
Capital																		
Capital Expenditures	NA	(71,547)	—	(40,645)	(42,763)	(44,777)	(45,367)	(45,962)	(46,559)	(47,158)	(47,760)	(48,364)	(48,969)	(49,576)	(50,185)			
Cash Flow Before Debt Service	\$843,843	\$859,176	\$883,948	\$772,254	\$812,498	\$850,756	\$861,979	\$873,285	\$884,620	\$896,005	\$907,435	\$918,907	\$930,414	\$941,953	\$953,518			
CapEx % NOI	—	7.7%	—	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%			
Unlevered Cash Flow																		
Purchase Property				(\$17,000,000)	—	—	—	—	—	—	—	—	—	—	—			
Purchase Cost				(255,000)														
Cash Flow before Debt Service				—	812,498	850,756	861,979	873,285	884,620	896,005	907,435	918,907	930,414	941,953	—			
Exit Value				—	—	—	—	—	—	—	—	—	—	11,808,269	—			
Exit Cost				—	—	—	—	—	—	—	—	—	—	(177,124)	—			
Unlevered Cash Flow				(\$17,255,000)	\$812,498	\$850,756	\$861,979	\$873,285	\$884,620	\$896,005	\$907,435	\$918,907	\$930,414	\$12,573,099	—			
IRR				2.18%														
MoC				1.19x														

Rent vs. Buy Analysis

The least capital-intensive solution would be to continue renting. You could invest \$9.5M into a low-risk investment fund yielding 5.75%, from which you could pay your rent annually.

- Alternatively, you could purchase the property for \$13.2M (inclusive of purchase costs) and expect a similar return on investment (5.75% annually over 10 years).
- The \$13.2M assumes any deferred maintenance capital identified by 3rd party reports (PCA, Seismic, Environmental, etc.) is funded out of the \$13.2M gross purchase price. I highly recommend this stipulation given what appears to be limited historical capital improvement spend on the property.
- The \$17.0M asking price (\$17.3M including additional purchase cost estimates) would yield a significantly below-market return (2.18%), far beneath the rate you should expect from a high-yield savings account or government bonds.

	Historical		Projections										
Cash Flows	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
Projected Rent	Own %												
Manchester - 1st Floor Litigation	100.0%		\$460,346	\$469,571	\$478,963	\$488,551	\$498,322	\$508,288	\$518,454	\$528,823	\$539,399	\$550,187	
Manchester - 1st Floor Contracts	100.0%		40,366	41,175	41,999	42,839	43,696	44,570	45,461	46,371	47,298	48,244	
Manchester - 1st Floor Corporate Law	100.0%		94,474	96,367	98,295	100,262	102,267	104,313	106,399	108,527	110,698	112,912	
Manchester - Intellectual Property (2nd Floor)	100.0%		115,564	117,879	120,237	122,644	125,097	127,599	130,151	132,754	135,409	138,117	
Manchester - Employment Law (2nd Floor)	100.0%		81,066	82,691	84,345	86,033	87,754	89,509	91,299	93,125	94,987	96,887	
Manchester - Litigation Support (LL)	100.0%		55,235	56,341	57,468	58,619	59,791	60,987	62,207	63,451	64,720	66,014	
Manchester - Research (LL)	100.0%		28,887	29,466	30,056	30,657	31,270	31,896	32,534	33,184	33,848	34,525	
Manchester - Family Law (LL)	100.0%		38,359	39,127	39,910	40,709	41,523	42,353	43,200	44,064	44,946	45,845	
Manchester - Administrative (LL)	100.0%		171,731	175,172	178,676	182,253	185,898	189,616	193,408	197,276	201,222	205,246	
Surgery Partners - Auditorium	40.0%		68,032	69,396	70,784	72,201	73,645	75,117	76,620	78,152	79,715	81,310	
Surgery Partners - Storage Lower Level	40.0%		5,270	5,376	5,483	5,593	5,705	5,819	5,935	6,054	6,175	6,299	
Surgery Partners - Suite 207 2nd floor (Reception Area)	40.0%		11,637	11,869	12,107	12,349	12,596	12,848	13,105	13,367	13,634	13,907	
Value of Renting - 10 Year Cash Flow			(\$9,463,585)	\$1,170,967	\$1,194,432	\$1,218,320	\$1,242,709	\$1,267,563	\$1,292,914	\$1,318,772	\$1,345,148	\$1,372,051	\$1,399,492
Rent Growth %					2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%
Discount Rate / Return			5.75%										
NPV over 10 years			\$9,463,585										
Demonstration - Pay for Rent out of Investment Account													
Begin Balance			\$9,463,585	\$9,463,585	\$8,836,775	\$8,150,458	\$7,400,789	\$6,583,626	\$5,694,621	\$4,729,148	\$3,682,302	\$2,548,886	\$1,323,396
Returns			—	544,156	508,115	468,651	425,545	378,558	327,441	271,926	211,732	146,561	76,095
Pay Rent			—	(1,170,967)	(1,194,432)	(1,218,320)	(1,242,709)	(1,267,563)	(1,292,914)	(1,318,772)	(1,345,148)	(1,372,051)	(1,399,492)
Ending Balance			\$9,463,585	\$8,836,775	\$8,150,458	\$7,400,789	\$6,583,626	\$5,694,621	\$4,729,148	\$3,682,302	\$2,548,886	\$1,323,396	—
Offer Price at "Fair Value" - 10 Year Cash Flows			(\$13,217,918)	\$812,498	\$850,756	\$861,979	\$873,285	\$884,620	\$896,005	\$907,435	\$918,907	\$930,414	\$12,573,099
Discount Rate / Return			5.75%										
NPV over 10 years			\$13,217,918										
Ask Price at \$8.5M - 10 Year Cash Flows			(\$17,255,000)	\$812,498	\$850,756	\$861,979	\$873,285	\$884,620	\$896,005	\$907,435	\$918,907	\$930,414	\$12,573,099
Discount Rate / Return			2.18%										
NPV over 10 years			\$17,255,000										

- For comparability, the rent scenario assumes you rent for the next 10 years. The purchase scenarios both assume you purchase, hold, then sell after 10 years.

Appendix

High-Level Tax Strategies

Tax strategies are highly localized. I would suggest you explore strategies with a qualified tax advisor or accountant. That said, here are the most popular options that you will likely explore:

1. **1031 Exchange:** Also known as a like-kind exchange, a 1031 exchange allows you to defer capital gains taxes by reinvesting the proceeds from the sale of one property into the purchase of a similar, or “like-kind,” property within a specific time frame. Can also invest in funds if you don’t want the headache of managing a property. There are strict rules and deadlines to follow, so it’s crucial to work with a qualified intermediary and a tax advisor familiar with 1031 exchanges.
2. **Installment Sales / Seller Financing:** If Seller is willing to finance the Buyer’s purchase, they can use an installment sale to spread out their capital gains tax liability over several years. The client would receive payments over time, with each payment being partially taxed as capital gains.
3. **Opportunity Zones:** Believe this property is not located in an OZ, but these allow Seller to reinvest proceeds into a Qualified Opportunity Fund within 180 days of sale to defer capital gains.

Further Diligence Questions

1. How many renewal options does each tenant have? What are the terms of the renewal options?
2. Are there any major deferred capital items? Noting capex was zero in 2022 per the Cash Flow Statement.
3. Are there any major outstanding payables that the buyer would assume? TAs, LCs, Accounts Payable, etc.?
4. Are there any vacant units not shown on the January 1 rent roll, or is the building completely occupied?
5. What was the nature of the \$71,547 capital expense in 2021?
6. Is seller able to provide a Cash Flow statement for 2020? Trying to get a sense for steady-state capex
7. Are you able to provide budgeted expenses for 2023-2024?
8. Generally, what drove the 30.5% increase in expenses in 2022?
9. Cleaning Purchased Time: \$48.6k -> \$85.2k. Also, what is the nature of this expense?
10. What is the nature of admin purchased time? It seems to fluctuate from negative to positive
11. What was the 2021 legal expense associated with?
12. Why did property tax drop significantly in 2021?
13. What is the difference between "Taxes" and "Property Taxes"? Why has it been increasing so significantly in recent years?
14. Have you identified any backfill tenants to replace Sightline Law Group, PLLC? If so, are you able to share how far along the discussions are and any preliminary figures around Rent PSF, TIs, LCs, etc. to fill the space?
15. Has SRN Realty indicated any intent to vacate their space? Do you intend to increase their rent during your hold period?
16. How does the Seller currently manage the property? Are any third-party leasing brokers, property managers, etc. involved?
17. Does the annual increase of 2% or CPI for each tenant have a cap?
18. Which 2021 expense account in the income statement includes the \$2,221.86 of "Other Liabilities" that I see backed out in the 2021 Cash Flow Statement? Same question in 2022.

Suggested Next Steps

1. Run through this presentation as a group, explain key financial concepts driving the analysis
2. Review and potentially refine the assumptions driving the valuation model
3. Follow-up on diligence questions
4. Comparable sales analysis
5. Rental comps analysis