HIGHEST AND BEST USE ANALYSIS

FOR A SITE IN

ARLINGTON, VA

by
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The financial crisis began in 2007 and has irrevocably changed the global economy. Today, nations, businesses, and individuals alike are tasked with a deleveraging of gargantuan magnitude, in hopes to right their financial course in a turbulent and uncertain economy. This practicum explores a few of the questions a real estate owner is faced with given the aforementioned backdrop.

Debt is often used as a tool to leverage investors' returns particularly when it comes to real estate investments. However, debt carries with it a burden, investors must make periodic payments to retire or pay down their debt (depending on the type) and, upon maturity, an investor must retire their outstanding debt obligations, or risk losing their property.

This practicum assumes the role of an owner *"Luce Realty"* whose debt is maturing at 3701 N. Dr. Fairfax, in Arlington, Virginia. In order to best assess all possible options with regards to their asset at 3701 N. Fairfax. *Luce Realty* will conduct a highest and best use analysis of 3701 N. Fairfax that investigates the profitability and economic viability of (i) renovating the existing office building, (ii) developing a multi-family building or (iii) developing a hotel. The highest and best use analysis will compare the above mentioned options versus the outright sale of the property.

Site Analysis: 3701 N. Fairfax is located in the Rosslyn-Ballston Corridor of Arlington, Virginia. *Luce Realty* will perform a Site Analysis, a brief location overview and description of the site and its current improvements.

Zoning Analysis: *Luce Realty* will then investigate the potential development options allowed in accordance with Arlington County. The zoning analysis will also consider the legal and development requirements.

Market Analysis: The property is situated in Ballston a bustling, urban, live, work, play community. The area is populated by restaurants, bars, parks, schools, office buildings, mass transit options, numerous apartments and condominium high rises.

Luce Realty will perform a macro analysis on Arlington County, which will help ascertain the strength of future development. The Market Analysis section will delve into the history and characteristics of the area and will explain the reasons why this submarket is attractive to investors.

Market Feasibility Analysis: *Luce Realty* will provide market data on office buildings, multi-family buildings, and hotels, the three potential uses. This data will be used in the highest and best use underwriting. Additionally, the market feasibility analysis will outline some anticipated trends given the state of the Washington, DC real estate market.

Financial Analysis: The Financial Analysis section will be based on a highest and best use analysis that considers (i) renovating the existing office building, (ii) developing a multi-family building or (iii) developing a hotel. The highest and best analysis will consist of a three tiered approach, first it will consider a F.A.R. analysis, then use development costs and assumptions to create a development budget and thirdly use that budget to calculate a proforma. Once this three tiered approach is complete *Luce Realty* will have a return on cost metric to gauge the three developments.

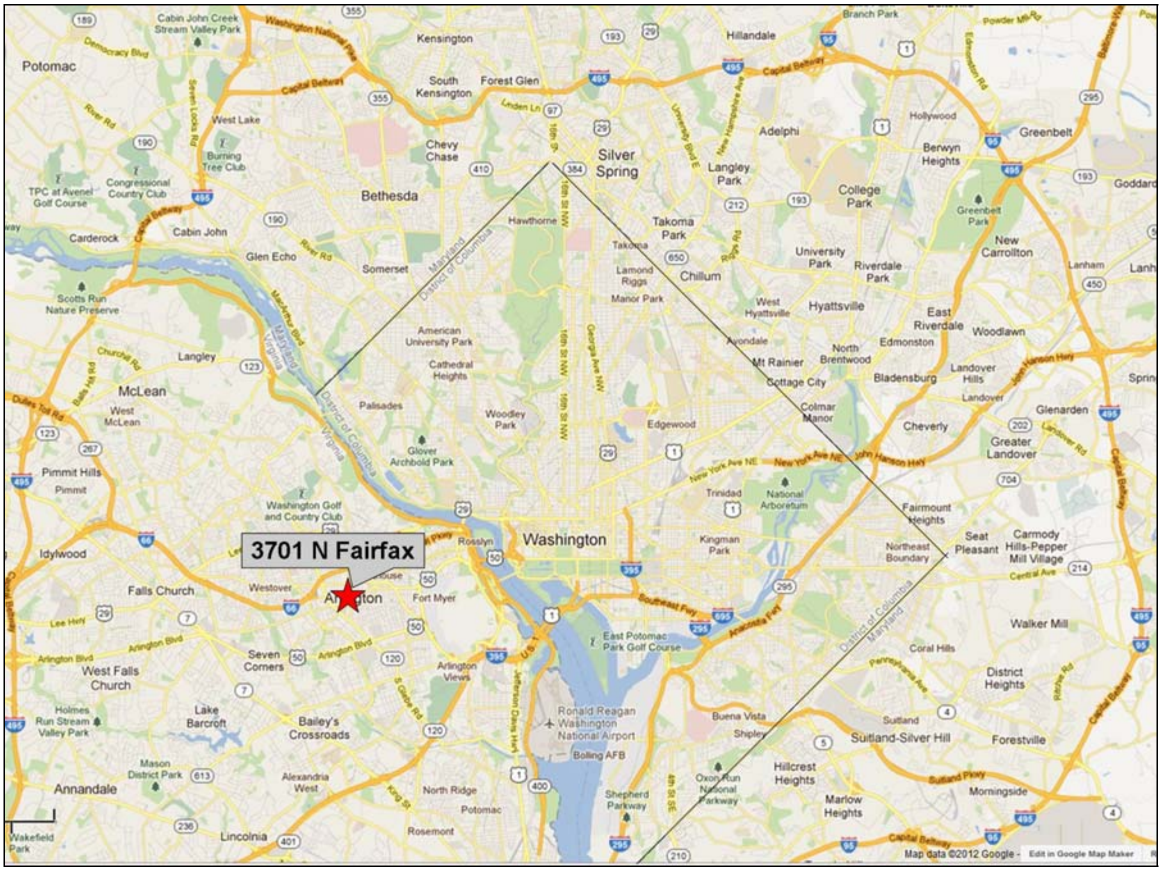
Alternatively, *Luce Realty* will consider the opportunity to sell the building today and see if the proceeds which could be recouped from a sale offset the maturing note.

Conclusion: This section will summarize findings of this practicum and come to a conclusion on the best course of action with regards *Luce Realty* and its asset at to 3701 N. Fairfax.

Iwo Jima Memorial

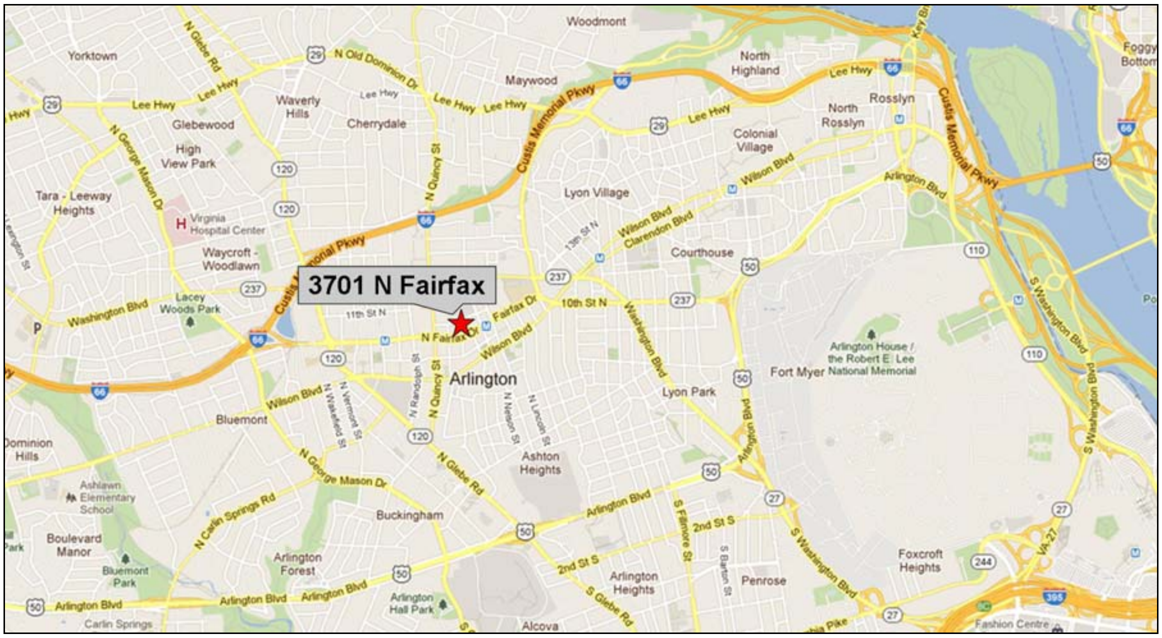
3701 N. Fairfax is located on the corner of North Nelson St. and North Fairfax Dr. in the heart of the Ballston/Virginia Square submarket in Arlington, Virginia. One of the biggest competitive advantages this site offers is that it is only one block from Virginia Square Metro station and its close proximity to Washington, DC, which is three miles awa. The Ballston/Virginia Square submarket encompasses approximately 260 acres of contiguous land.

<u>Map of Greater Washington DC</u>



Ballston/Virginia Square is considered a quintessential example of the new "urban village" offering a robust transit-oriented community. Two metro stations, Ballston and Virginia Square, and interstates 66 and 395 anchor the submarket offering accessibility to the Greater Washington area. Its vibrant business friendly environment is epitomized by the science, technology and trade associations that are located here. Its modern urban design is a model for "Smart Growth" and has led to Ballston becoming one of the most prominent submarkets in the nation. Its superb demographics are just one of the many evidences that illustrate this point. *(Source: Arlington Economic Development)*

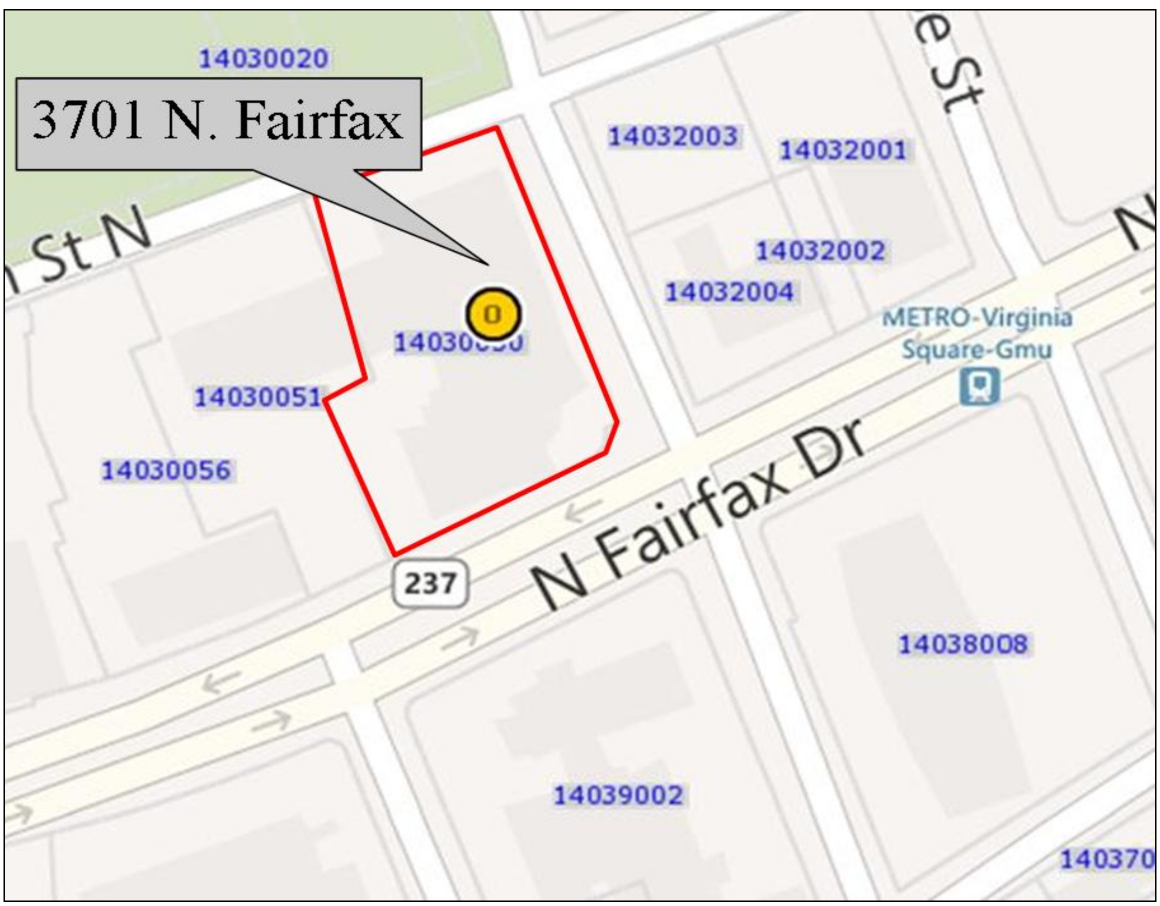
Map of Rosslyn-Ballston Corridor



Aerial of Ballston/Virginia Square

Birds-Eye View of Ballston/Virginia Square

3701 N Fairfax Parcel Map



Picture of 3701 N. Fairfax

The site upon which 3701 N. Fairfax is located includes 56,010 square feet or approximately 1.29 acres. 3701 N. Fairfax is currently improved by a nine story office building. The office building totals 182,000 square feet, which is currently completely vacant.

The signalized corner of Nelson Street and North Fairfax Drive is improved by a sidewalk and green space. The topography of the site is relatively level and offers no anticipated complications from a development standpoint.

3701 N. Fairfax entails two levels of below-grade parking and a surface parking lot, which totals 296 spaces. 256 spaces are below-grade and 40 spaces are surface parked. The building is also served by four elevators and two sets of interior stairwells. The HVAC system for 3701 N. Fairfax has two cooling towers and supplemental packages on the roof.

3701 N. Fairfax was built using reinforced concrete for the foundation and floors. The exterior of the building is aluminum frame with glass paneling and the roof is flat with an asphalt cover.

3701 N. Fairfax is zoned C-O-A, which is a commercial, office, and apartment district. According to the Arlington County Zoning Ordinance the purpose of the C-O-A zone is to stimulate a coordinated mixed-use development of office, apartment and hotel uses in the vicinity of metro-rail stations. Determination of the actual types and densities of uses will be via a site plan approval process based on site characteristics, maximum densities and heights. The need for community facilities, open spaces, landscaped areas and circulation utilities will also be considered when determining density and heights. *(Source: The Zoning Ordinance: Planning Division: Arlington, Virginia)*

A more intensive review of the site including discussions, Jim Connell of Arlington County shows that 3701 N. Fairfax is governed by a special exception, site plan 46. According to a BZA Staff Report “Exhibit A” found in the Arlington County Zoning Office site plan 46 was approved on May, 2, 1964. The intent of Site Plan 46 implies that the total gross area should not exceed a floor area ratio of 3.25 which would theoretically permit development of a property including 182,032 (56,010 x 3.25) square feet. However a more detailed analysis is required to determine the maximum allowable building that can be developed on the site.

The 182,000 allowed per site plan 46, is greater then the current zoning maximum densities per the C-O-A “Exhibit B” zoning further described in this section. However, given the current use and size of the building (office and 182,000 SF), per site plan 46, it is reasonable to assume that upon an office renovation an owner would be able to build to the same existing density. The land area for the property is 56,010 square feet or approximately 1.29 acres. The applicable F.A.R. is governed by the site area as demonstrated in the table below.

<u>Site Area Table</u>

Site Area	Maximum Total Floor Area Ratio	Maximum Office Hotel and Commercial Floor
4,999 sq. ft. or below	1.00	0.50
5,000 sq. ft.	1.50	0.75
10,000 sq. ft.	2.00	1.00
15,000 sq. ft.	2.50	1.25
20,000 sq. ft.	3.00	1.50
30,000 sq. ft.	3.50	1.75
40,000 sq. ft.	4.00	2.00
50,000 sq. ft	4.50	2.25
60,000 sq. ft	5.00	2.50
70, 000 sq. ft	5.50	2.75
80,000 sq. ft. and above	6.00	3.00

Sites with more than twenty thousand (20,000) square feet and less than eighty thousand (80,000) square feet which do not have the precise number of square feet shown on the table above, the F.A.R. shall be the F.A.R. allowed for the next smaller site shown on the table plus .00005 maximum total F.A.R. for each additional square foot of site area. The maximum office, hotel, and commercial F.A.R. to be added for each square foot shall be .000025. The math for this is outlined in supplemental site area table below. *(Source: "SECTION 25A."C-O-A" COMMERCIAL, OFFICE AND APARTMENT DISTRICTS)*

Supplemental Site Area Table

Site	Additional FAR	Maximum Total Floor Area Ratio	Maximum Square Feet	Additional FAR	Maximum Office Hotel and Commercial Floor	Maximum Office Hotel and Square Feet
50,000		4.50	225,000		2.25	112,500
6,010	0.00005	0.30	1,806	0.000025	0.15	903
56,010		4.80	268,876		2.40	134,438

As a means to encourage apartment development, an additional one-half (1/2) F.A.R. may be approved within any project that is at least ninety percent committed to apartments. Assuming that ninety percent of the project is committed to apartments, this would bring the F.A.R. to (4.80 + .05) 5.30 and maximize density at 296,881 as seen in the bonus residential F.A.R. table below. *(Source: "SECTION 25A."C-O-A" COMMERCIAL, OFFICE AND APARTMENT DISTRICTS)*

Bonus Residential FAR Table

Site	FAR	Maximum Square Feet
56,010	5.30	296,881

The “C-O-A” zoning is restricted by the height limitation table shown below.

“C-O-A” Height Limit Table

Site	Office and Hotel	Apartment
19,999 sq. ft. or below	100 feet	151 feet
20,000 to 29,999 sq. ft.	110 feet	162 feet
30,000 to 39,999 sq. ft.	120 feet	171 feet
40,000 to 49, 999 sq. ft.	130 feet	180 feet
50,000 to 59,999 sq. ft.	140 feet	189 feet
60,000 to 69,999 sq. ft.	150 feet	198 feet
70,000 to 79,999 sq. ft.	160 feet	207 feet
80,000 sq. ft. and above	170 feet	216 feet

Landscaping

A minimum of ten percent of the total site area is required to be landscaped open space in accordance with the requirements of Section 32A of the Arlington County Zoning Ordnance. All developments considered in the highest and best use analysis will include 5,601 square feet of space dedicated to green space. *(Source: "SECTION 25A."C-O-A" COMMERCIAL, OFFICE AND APARTMENT DISTRICTS)*

Parking Requirements

The parking requirements are outlined below based on use:

1. One off street parking space shall be provided for each dwelling unit. (344 x 1 = 344 parking spaces)

2. One parking space is required for each five hundred thirty square feet of commercial or office space. (182,000 / 530 = 343 parking spaces)

3. One parking space per hotel unit (199 x 1 = 199 parking spaces)

(Source: "SECTION 25A."C-O-A" COMMERCIAL, OFFICE AND APARTMENT DISTRICTS)

Approval Process

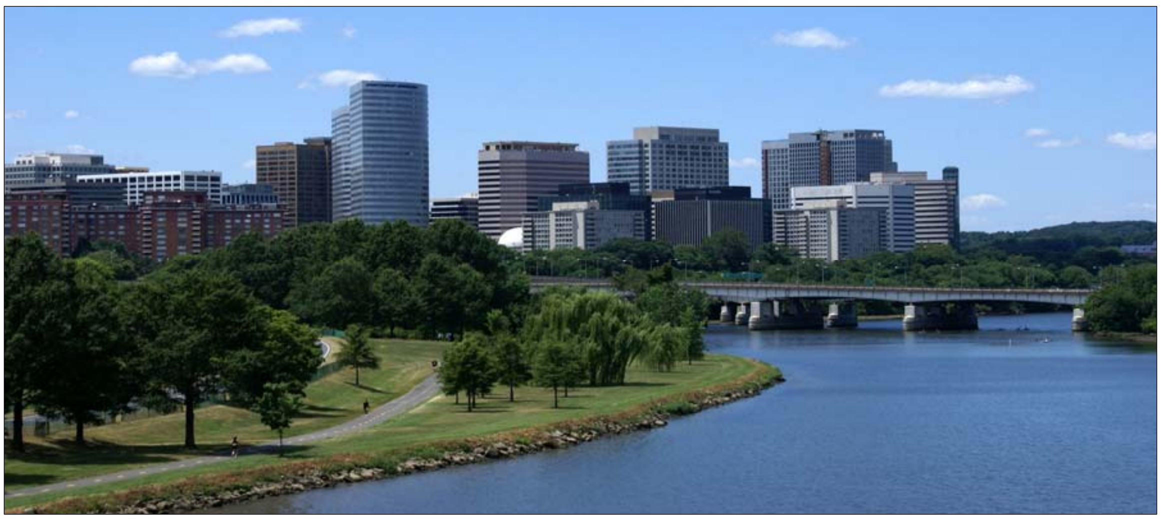
Per section 36 of the Arlington County Zoning Ordinance, the process for obtaining site plan approval in Arlington County requires a public hearing from the County Board to determine that the improvement and development proposed by the site plan: (a) substantially complies with the character of master plans and regulations (b) functionally relates to other structures permitted in the neighborhood (c) is so designed and located that the public health, safety and welfare will be promoted and protected. *(Source: "SECTION 36. ADMINISTRATION AND PROCEDURES.")*

Conclusion

To recap the zoning analysis it is anticipated that both (i) a renovated office building and (ii) hotel can be built to the site plan 46 approved 3.25 FAR which equates to 182,033 square feet, while (iii) a multi-family building can be built to 5.30 FAR which equates to 296,853 in accordance with the “C-O-A” zoning.

3701 N. Fairfax is located in the Rosslyn-Ballston Corridor "R-B Corridor" of Arlington County. In terms of land area, Arlington County is the smallest county in Virginia, however it is also one of the most populated counties with over 200,000 residents. Arlington County has a long standing history with the District of Columbia given its close proximity. Arlington County is home to several federal establishments most notably the Pentagon, Arlington National Cemetery, Fort Myer, and Reagan International Airport. The location of the Pentagon and its federal counterparts has been instrumental in the growth of Arlington. *(Source: Urban Amenities)*

<u>View of Rosslyn from the Potomac River</u>



Ballston/Virginia Square History

Ballston has a deep routed history, its most prominent intersection North Glebe Road and Wilson Boulevard, was once known as Balls Crossroads, is one of the oldest crossroads in Northern Virginia and dates back to the 1740's. By 1896 an electric trolley took passengers from present day Ballston into Washington DC. In November 1951, Parkington Shopping Center was developed, the headquarters of the Hecht Company anchored the Center. Ballston has hence forth been considered a retail hub. *(Source: History of Arlington)*

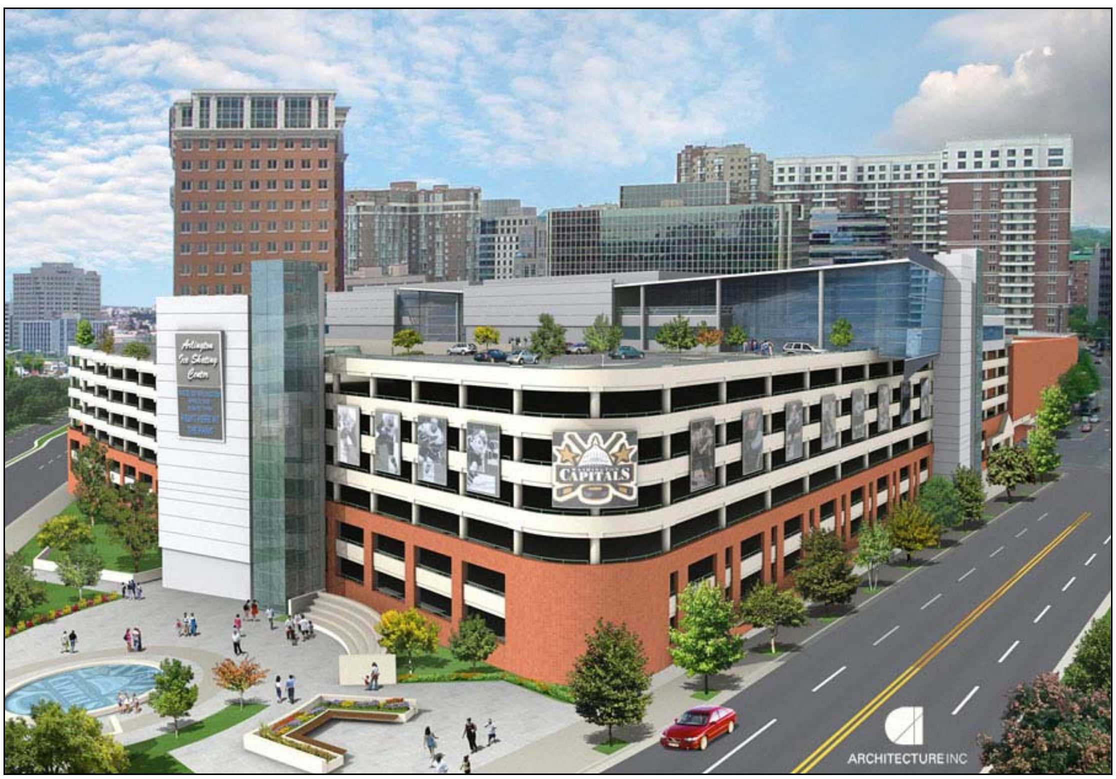
The Washington Metropolitan Area Transit opened the Ballston Metro station on December 1, 1979. The Ballston Metro Station is the western anchor to the "R-B Corridor". Starting west, heading east into Washington, DC the R-B Corridor consists of five metro stations: Ballston Metro Station, Virginia Square Metro Station, Clarendon Metro Station, Courthouse Metro Station and Rosslyn Metro Station. The R-B Corridor is often considered an extension of the District of Columbia as it is located just over the Potomac River. The R-B Corridor has the highest density of mixed-use development in Arlington County and is often praised for its balance of hotel, retail, residential and office development. This dynamic mix, with its 24-hour environment has truly made the R-B Corridor a preferred submarket. *(Source: History of Arlington & Urban Amenities)*

Ballston Metro Station

Adopted by the County in 1980, the Ballston Sector Plan sought to create a “new downtown” in central Arlington. The land use and development guidelines adopted for Ballston were implemented to facilitate the creation of a dynamic downtown area by ensuring that development would include a mix of commercial, office and residential uses. The Concept Plan that was adopted as part of the Ballston Sector Plan providing a vision of a future urban environment.
(Source: Ballston Metro Station Area)

The Concept Plan’s recommendations that have been implemented successfully include the redevelopment of Parkington Shopping Center as Ballston Common Shopping Mall. Today, the Ballston Common Shopping Mall is also home to Kettler Ice-Plex, which features two ice rinks for public and private use. Kettler Ice-Plex also serves as the practice facilities for the Washington Capitals, the local professional hockey team.
(Source: Ballston Metro Station Area and Kettler)

Kettler Ice-Plex @ Ballston Commons Mall



Jobs and Demographics

The 2011 Arlington, Virginia Profile indicates that Arlington County is home to 210,000 jobs. The county boasts a vibrant workforce, originally anchored by government agencies (Dept of Labor, Navy, State, USPS and DARPA) the work force has since evolved into the forefront of the technology and commerce industries. Specifically, Ballston is, home to organizations including: The National Science Foundation, CACI International, SAIC, Office of Navy Research and E*Trade Bank. (Source: Arlington, Virginia Profile 2011)

Arlington's recent accolades include:

- Named America's Second Best City – Bloomberg, 2011
- Named the second healthiest County in Virginia - County Health Rankings, 2011
- Named Ninth Richest County – Forbes, 2010
- Hailed as an "oasis of stability amid a downturn" – New York Times, 2009

According to the Arlington Economic Development, the county boasts the highest concentration of 22-34 year olds in the region and the most highly educated community in Washington, DC with 70% of Arlingtonians holding bachelors degrees and over a quarter holding advanced degrees. *(Source: Arlington Demographics & Workforce)*

Radius Demographics from 3701 N. Fairfax

Radius	1 Mile	3 Mile	5 Mile
Population:			
2015 Projection	43,252	252,492	617,850
2010 Estimate	38,417	237,434	588,154
2000 Census	29,852	215,592	539,536
Growth 2010-2015	12.60%	6.30%	5.00%
Growth 2000-2010	28.70%	10.10%	9.00%
2010 Households:			
2015 Projection	20,739	107,486	280,080
2010 Estimate	18,411	100,904	266,895
2000 Census	14,114	92,258	247,442
Growth 2010-2015	12.60%	6.50%	4.90%
Growth 2000-2010	30.40%	9.40%	7.90%
Owner Occupied	7,385	42,735	114,100
Renter Occupied	11,026	58,169	152,796
2010 Avg Household Income	**$113,257**	**$104,251**	**$105,326**
2010 Med Household Income	**$92,516**	**$81,838**	**$78,047**
2010 Per Capita Income	**$54,760**	**$44,954**	**$48,340**

(Source: CoStar)

Development

Driven by "Smart Growth" development Ballston has become a vibrant mix of office, residential, retail and hotel uses. Ballston is typically business by day and sociable by night with numerous restaurants and other entertainment spots for residents and employees offering a truly "live, work, play" environment.

Ballston - Development Summary			
	Existing	Under Construction	Approved Not Built
Office (sq ft)	6,624,008	771,346	418,810
Housing Units	6,053	90	522
Hotel Rooms	892	0	183
Retail (sq ft)	1,025,913	36,241	27,785

(Source: Arlington Economic Development)

According to the *Arlington Economic Development Fourth Quarter 2011 Development Summary* Ballston hast two buildings under construction 800 N. Glebe and Founder's Square. 800 N. Glebe is a 282,989 speculative office building being developed by JBG, with an anticipated delivery date second quarter of 2012. LEED Gold certified, 800 N. Glebe will be located at the North East quadrant of the intersection of N. Glebe Rd. and Wilson Blvd, the old Balls Crossroads. On September 13, 2011 *The Washington Business Journal* announced *JBG* had leased 100,000 SF to Accenture at 800 N Glebe. *(Source: Arlington Economic Development and Accenture signs Ballston lease with JBG - Washington Business Journal.)*

<u>800 N. Glebe Rd</u>

Directly across the street from Ballston Mall, Founders Square will consist of four buildings, the *Shooshan Company* is slated to build the first two, one office and one hotel. The secure office building will deliver in the first quarter of 2012 and is a build-to-suit for the Defense Advanced Research Projects Agency (DARPA). *(Source: Arlington Economic Development)*

Founders Square

Conclusion

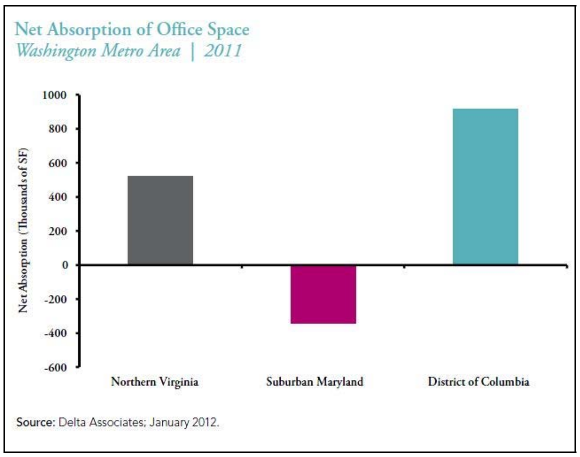
3701 N. Fairfax is situated in one of the fastest growing areas of the Washington, D.C. metropolitan region which offers it a tremendous competitive advantage. Today the R-B Corridor is widely considered one of the healthiest markets in the nation as witnessed by the mass transit options, its long standing history with the Nation's Capital, which has in turn lead to a strong employment base in a neighborhood with some of the strongest demographics in the area. The R-B Corridor's continued growth and new development will only reinforce the presence of this flourishing market.

To properly underwrite the highest and best use analysis *Luce Realty* conducted a Market Feasibility Report for the Washington DC MSA and more specifically the Ballston Submarket for the three considered uses i) office ii) multi-family and iii) hotel.

Office Market Feasibility

As provided in the 2012 TrendLines Report published by Delta Associates and Transwestern, the Washington Metro Area is the third largest office market in the nation at 401 million square feet. The Washington Metro Area absorbed a net of 1.1 million of square feet in 2011, the leasing market was not as robust as it has been in previous years due to several sizable tenants vacating space as evidenced in the graph below. *(Source: 2012 Trendlines)*

Washington Metro Area 2011 Office Net Absorption Graph



The following is a list of large tenant which vacated space in the R-B Corridor last year, hampering net absorption. *(Source: 2012 Trendlines)*

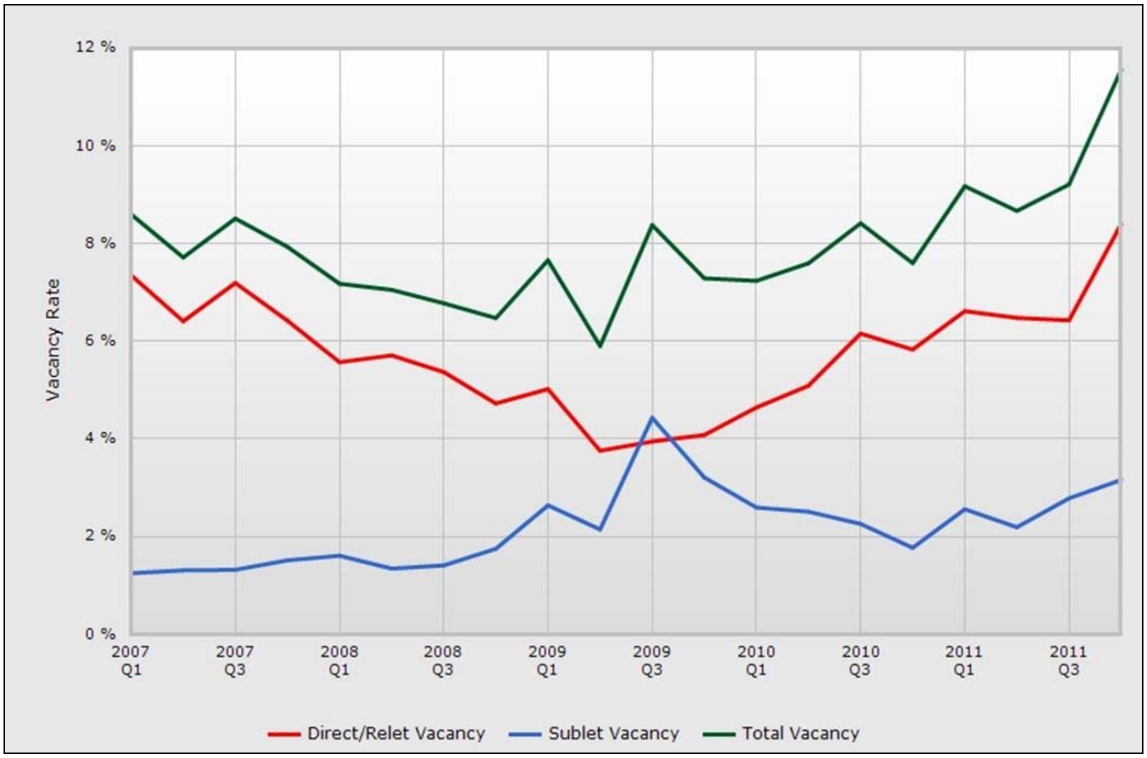
Tenant	Square Footage	Address
Verizon	300,000	1320 N. Courthouse Rd.
US Air Force	160,000	1500 Wilson Blvd.
American Chemistry Council	147,000	1300 Wilson Blvd.
Arlington County Health/Human Services	134,000	3033 Wilson Blvd.

At of the end of 2011 there were 1,052 buildings with blocks of space available over 100,000 square feet. As this space is absorbed, the Washington Metro Area will move toward equilibrium from a fundamental supply and demand sentiment. Trendlines expects the Washington Metro Market to remain one of the best performing office markets in the nation for the short and long term, however the rebalancing of the Federal budget could create some short term inefficiencies. From an investor standpoint Trendlines believes the biggest opportunities currently lie in 1) accumulating assets below replacement costs in an attractive interest rates environment and 2) repositioning older, under performing assets at superior locations (i.e. 3701 N. Fairfax). *(Source: 2012 Trendlines)*

According to CoStar, the R-B Corridor consists of nearly 16 million square feet of Class A office space with a direct/relet vacancy rate of just 8%. The average asking rental rate for office space in this submarket is $44.65 per square foot on a full service basis. *(Source: CoStar)*

The chart below illustrates the durability and consistency of this submarket over the last five years from an occupancy standpoint during a soft economic environment.

Class A Office Vacancy Chart in the R-B Corridor



(S*ource: CoStar)*

The chart above shows a recent uptick in the vacancy rate due to two market factors. First, the recent construction of speculative office buildings is increasing the supply of office buildings in the submarket. Second, the Base Realignment and Closure (BRAC) has a critical impact on office tenants in the market. Federal agencies are being relocated by BRAC and their federal contracting counterparts are following suit. Federal contractors are often contractually obligated to be in close proximity to the agencies their businesses serve. This exodus of office tenants is causing a glut of available space in the market. (S*ource: CoStar and Defense Base Closure and Realignment Commission)*

As discussed in the *Wall Street Journal* article “Corporate Cram Bedevils Office Recovery” dated February 29, 2012; businesses are attempting to run more efficiently. One example of this efficiency measure is that businesses are seeking smaller offices, in which they will pack more employees into less space. This is a long term negative for the office industry. *(Source: Corporate Cram Bedevils Office Recovery - WSJ)*

The below rent comps are indicative of terms, which a new tenant leasing space in the R-B Corridor should expect, these comps along with the Costar research will drive the assumptions in *Luce Realty's* highest and best use analysis.

Rent Comparables

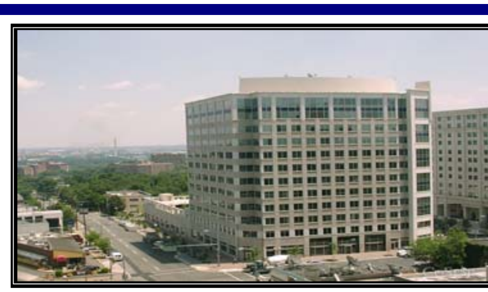
Name	One Virginia Square		
Address	3601 Wilson Boulevard		
City, State	Arlington, VA		
Year Built:	1999	**Date:**	6/28/2011
Tenant:	System Planning Corporation		
Tenant SF:	116,077		
Rental Rate:	$42.91	**Term:**	9.8 years
Expense:	Full Service	**TI's:**	$30.00
Escalation:	2.75%	**Abatement:**	2 Months

Name	Elipse @ Ballston Phase I		
Address	4350 N Fairfax Drive		
City, State	Arlington, VA		
Year Built:	1989	**Date:**	6/22/2011
Tenant:	Doyle & Bachman		
Tenant SF:	3,040		
Rental Rate:	$38.00	**Term:**	5.3 Years
Expense:	Full Service	**TI's:**	As-Is
Escalation:	3.00%	**Abatement:**	None

Name	Fairgate @ Ballston Phase I		
Address	1005 N Glebe Road		
City, State	Arlington, VA		
Year Built:	1988	**Date:**	6/17/2011
Tenant:	National Grocers Association		
Tenant SF:	7,558		
Rental Rate:	$37.25	**Term:**	10.1 Years
Expense:	Full Service	**TI's:**	$20.00
Escalation:	3.00%	**Abatement:**	1 Month

Name	The Hartford Building		
Address	3101 Wilson Boulevard		
City, State	Arlington, VA		
Year Built:	2004	**Date:**	5/1/2011
Tenant:	Aecom		
Tenant SF:	24,550		
Rental Rate:	$44.00	**Term:**	10 Years
Expense:	Full Service	**TI's:**	Turnkey
Escalation:	2.50%	**Abatement:**	None

Name	Courthouse Tower		
Address	1515 N Courthouse Road		
City, State	Arlington, VA		
Year Built:	1999	**Date:**	5/1/2011
Tenant:	Charles G. Kock Charitable Foundation		
Tenant SF:	42,657		
Rental Rate:	$43.50	**Term:**	2.1 Years
Expense:	Full Service	**TI's:**	$20.00
Escalation:	2.75%	**Abatement:**	None



**Rent comps provided by Cassidy Turley*

Sales Comparables

Name	One Virginia Square		
Address	3601-3611 Wilson Blvd		
City, State	Arlington, VA		
SF:	116,077	Date:	11/7/2011
Leased:	100%	Price:	$61,850,000
Built:	1999	$/SF:	$533
		Cap Rate:	6.00%
Buyer:	LaSalle Investment Management		
Seller:	TIAA-CREF		

Name	The Architect Building		
Address	1400 Wilson Blvd		
City, State	Arlington, VA		
SF:	108,296	Date:	11/9/2011
Leased:	100%	Price:	$52,650,000
Built:	1965	$/SF:	$486
		Cap Rate:	6.06%
Buyer:	Salus Property Investments		
Seller:	Great Point Investors		

Name	The Hartford Building		
Address	3101 Wilson Blvd		
City, State	Arlington, VA		
SF:	212,443	Date:	12/17/2010
Leased:	100%	Price:	$112,600,000
Built:	2004	$/SF:	$530
		Cap Rate:	5.70%
Buyer:	Heitman		
Seller:	Angelo Gordon & Co.		

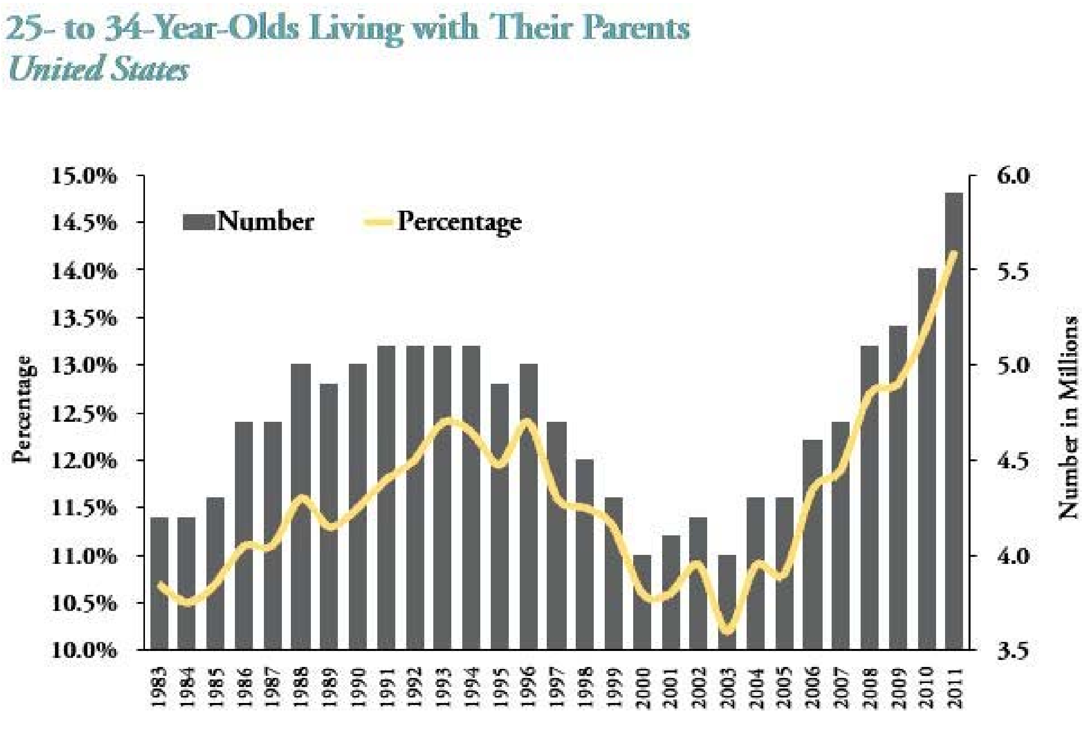
**Sales Comps provided by CoStar*

Multi-Family Market Feasibility

As provided in the TrendLines Report published by Delta Associates and Transwestern, apartment market in the Washington Metro Area is one of the strongest in the U.S. Rents had spiked 8.2% in 2010 while units absorbed at record numbers for the market. As of December 2011 the vacancy rate for the Washington Metro area was 3.8%. *(Source: 2012 Trendlines)*

Trenlines also notes that there is substantial pent up rental demand due to the amount of young adults (25-34 years old) living at home, as a result of the recent recession. Currently in the U.S., 5.5 million 25-34 year olds live at home representing a huge pool of likely renters, as shown in the graph below. *(Source: 2012 Trendlines)*

25-34 Year Olds Living with their Parents in the US



Source: U.S. Census Bureau, John Burns Real Estate Consulting, Delta Associates; January 2012.

The large stock of renters expected to emerge from 2010 through 2015, totals nearly 9.1 million, three times more then the nation experienced from 2005 to 2010. Young adults moving out of their parents house, coupled with the psychological fear associated with owning a home following the national housing collapse will attribute to this stock. This pool of renters should bolster the demand and strengthen the apartment market for the foreseeable future. *(Source: 2012 Trendlines)*

As published in the *Washington Post*, with research from *Delta Associates, C*lass A apartments in Rosslyn-Ballston saw rents grow an average of 4.6 percent in 2011 with vacancy declining from 4 percent to 3 percent during the year. The pipeline of new units grew to 2,723 units at the end of 2011, up from 1,896 a year earlier. Effective rents for Class A units averaged $2,308 a month, with concessions representing 2.1 percent of face rents. The Class A apartment market is likely to remain strong in 2012, given the low vacancy rate, but new buildings coming on line will begin to impact the market by 2013. *(Source: Delta: Strong market conditions in Rosslyn-Ballston corridor - Washington Post)*

Rent Comps

Lease Comparables

Name		Lyon Place at Clarendon Center		
Address		1200 N. Garfield		
City, State		Arlington, VA		
		Average Unit Mix		
Type	No.	Square Footage	Rent	Rent P/SF
Studio	18	450	$1,767	3.93
1BR	168	760	$2,675	3.52
2BR	56	1035	$3,188	3.08
3BR	2	1356	$4,597	3.39
Total	**244**	**187,537**	**$2,550**	**$3.32**

Name		Zoso Flats		
Address		1025 N. Fillmore Street		
City, State		Arlington, VA		
		Average Unit Mix		
Type	No.	Square Footage	Rent	Rent P/SF
Studio	5	615	$2,048	3.33
1BR	80	800	$2,544	3.18
2BR	29	1300	$3,445	2.65
Total	**114**	**106,967**	**$2,818**	**$3.00**

Name		Quincy Plaza		
Address		3900 Fairfax Dr.		
City, State		Arlington, VA		
		Average Unit Mix		
Type	No.	Square Footage	Rent	Rent P/SF
1BR	320	780	$2,106	2.70
2BR	148	1080	$2,689	2.49
3BR	31	1375	$3,836	2.79
Total	**499**	**430,815**	**$2,241**	**$2.60**

**Lease Comps provided by CBRE*

Hotel Market Feasibility

According to Hotel Horizons with data collected from Smith Travel Research, Washington was not impacted as significantly as the national average during the financial crisis, due to the federal government mitigating the cyclical business environment. Below is a historical and forecast summary for the Greater Washington Area. *(Source: Hotel Horizons)*

Hotel Forecast Summary Table

FORECAST SUMMARY

Year	Occ	Δ Occ	ADR	Δ ADR	RevPAR	Δ RevPAR
2006	68.3%	-4.2%	$141.74	7.4%	$96.82	2.9%
2007	68.2%	-0.1%	$149.96	5.8%	$102.33	5.7%
2008	66.9%	-2.0%	$153.47	2.3%	$102.61	0.3%
2009	64.6%	-3.4%	$145.28	-5.3%	$93.82	-8.6%
2010	67.0%	3.8%	$143.45	-1.3%	$96.13	2.5%
2011F	67.2%	0.3%	$145.98	1.8%	$98.08	2.0%
2012F	68.2%	1.5%	$150.11	2.8%	$102.35	4.4%
2013F	69.3%	1.7%	$157.95	5.2%	$109.51	7.0%
2014F	69.4%	0.1%	$164.37	4.1%	$114.11	4.2%
2015F	68.8%	-0.9%	$169.70	3.2%	$116.81	2.4%

Source: PKF Hospitality Research, Smith Travel Research

Long Run Averages - 1988 to 2010		
Occupancy: 67.5%	Δ ADR: 3.2%	Δ RevPAR: 3.2%

Source: Smith Travel Research

(Source: Hotel Horizons)

Also provided by Smith Travel Research, the below Arlington Submarket Profile offers an substantial overview of the market and provides the projected occupancy, average daily room rate (ADR) and revenue per available room (RevPar) which will be used in *Luce Realty's* highest and best use analysis. *(Source: Hotel Horizons)*

Submarket Profile - Arlington

Total Rooms: 10,882

The Arlington hotel submarket consists of hotels located in the city of Arlington, Virginia. This includes properties located near Reagan National Airport.

Submarket Rank*

8

Out of 10

*Based on RevPAR change over the last 4 quarters.

Submarket Penetration*

122%

*Submarket RevPAR penetration expressed as a percentage of the market RevPAR for the previous 4 quarters. Direction of arrow indicates if penetration is increasing or decreasing relative to one year ago's performance.

Arlington Submarket Inventory

Upper-Priced	Properties	Rooms	% Submkt.	Lower-Priced	Properties	Rooms	% Submkt.
Inventory	26	8,286	76.1%	Inventory	19	2,596	23.9%
Upper-Priced Brands by Share	**Properties**	**Rooms**	**% Submkt.**	**Lower-Priced Brands By Share**	**Properties**	**Rooms**	**% Submkt.**
Marriott	3	1,622	14.9%	Holiday Inn	3	808	7.4%
Hyatt	2	1,003	9.2%	Best Western	2	346	3.2%
Residence Inn	4	976	9.0%	Comfort Inn	2	246	2.3%

Source: Smith Travel Research

Arlington Construction Pipeline

	Upper-Priced			Lower-Priced			Unclassified / Independent		
Phase	Properties	Rooms	% Submkt.	Properties	Rooms	% Submkt.	Properties	Rooms	% Submkt.
Pre-Planning	0	0	0.0%	0	0	0.0%	0	0	0.0%
Planning	0	0	0.0%	0	0	0.0%	0	0	0.0%
Final Planning	1	183	1.7%	1	136	1.2%	0	0	0.0%
In Construction	0	0	0.0%	0	0	0.0%	0	0	0.0%
Total	**1**	**183**	**1.7%**	**1**	**136**	**1.2%**	**0**	**0**	**0.0%**

Source: Dodge / TWR / STR / PKF-HR

Arlington Performance - All Hotels

Year	Occ	Δ Occ	ADR	Δ ADR	RevPAR	Δ RevPAR
2006	72.9%	-2.2%	$155.81	10.1%	$113.56	7.6%
2007	74.1%	1.6%	$162.88	4.5%	$120.66	6.3%
2008	72.6%	-2.0%	$168.97	3.7%	$122.60	1.6%
2009	71.4%	-1.5%	$164.04	-2.9%	$117.19	-4.4%
2010	73.3%	2.6%	$163.69	-0.2%	$120.03	2.4%
2Q10 YTD	75.6%	0.5%	$169.47	-1.8%	$128.16	-1.3%
2Q11 YTD	74.8%	-1.0%	$167.63	-1.1%	$125.46	-2.1%

All Hotels Penetration vs. Market Total

Year	Occ	ADR	RevPAR
2006	106.7%	109.9%	117.3%
2007	108.6%	108.6%	117.9%
2008	108.5%	110.1%	119.5%
2009	110.6%	112.9%	124.9%
2010	109.4%	114.1%	124.9%
2Q10 YTD	111.1%	114.9%	127.7%
2Q11 YTD	110.2%	111.5%	122.9%

Source: Smith Travel Research

Arlington Performance - Upper-Priced Hotels

Year	Occ	Δ Occ	ADR	Δ ADR	RevPAR	Δ RevPAR
2006	74.3%	-4.1%	$164.99	9.6%	$122.62	5.1%
2007	76.3%	2.7%	$172.12	4.3%	$131.34	7.1%
2008	73.9%	-3.2%	$178.85	3.9%	$132.17	0.6%
2009	73.4%	-0.6%	$173.36	-3.1%	$127.28	-3.7%
2010	75.3%	2.5%	$172.13	-0.7%	$129.55	1.8%
2Q10 YTD	77.7%	0.1%	$178.68	-1.7%	$138.82	-1.6%
2Q11 YTD	76.7%	-1.3%	$175.93	-1.5%	$134.89	-2.8%

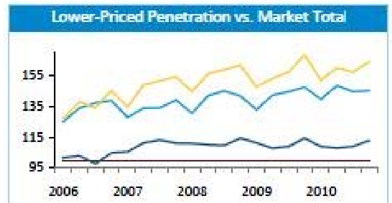
Upper-Priced Penetration vs. Market Total

Arlington Performance - Lower-Priced Hotels

Year	Occ	Δ Occ	ADR	Δ ADR	RevPAR	Δ RevPAR
2006	68.0%	2.4%	$121.78	8.2%	$82.80	10.9%
2007	67.0%	-1.5%	$129.40	6.3%	$86.68	4.7%
2008	68.2%	1.8%	$134.19	3.7%	$91.54	5.6%
2009	64.9%	-4.8%	$129.38	-3.6%	$84.01	-8.2%
2010	66.8%	2.9%	$131.44	1.6%	$87.78	4.5%
2Q10 YTD	68.6%	1.9%	$134.15	-2.8%	$92.03	-1.0%
2Q11 YTD	68.3%	-0.4%	$134.38	0.2%	$91.81	-0.2%

Source: Smith Travel Research

Lower-Priced Penetration vs. Market Total



Source: Smith Travel Research

(Source: Hotel Horizons)

3701 N. Fairfax is encumbered by a maturing note of $45,000,000 for a building that is entirely vacant. This predicament requires *Luce Realty* to make a decision on the best course of action for its real estate asset. To fully understand all options *Luce Realty* conducted a "back of the envelope" highest and best use analysis to determine whether (i) an office building renovation, (ii) a multi-family development or (iii) a hotel development is the most economically viable use for the site at 3701 N. Fairfax. Then *Luce Realty* compared that to the prospect of a sale of the property.

The "back of the envelope" involved a three tier approach; first the maximum density for each use was determined in accordance with the zoning analysis. Next, *Luce Realty,* reached out to John Fitzgerald, Regional Director of Development of the *Archon Group* to help provide cost estimates for the three proposed uses. Development costs have been outlined in the highest and best use analysis contained herein.

Subsequently, *Luce Realty* consulted with Bill Wrench, Chief Underwriter at *Phillips Realty Capital* to help ascertain market income, expense and debt assumptions, which have been outlined in the analysis to deduce a proforma or un-trended net operating income for each use (anticipated net operating income if the building was built and operational today).

Capital Markets Overview

The capital markets have historically dictated the direction of the real estate industry. Today is no different. The future success of 3701 N. Fairfax will be directly correlated to the capital markets. Given that 3701 N. Fairfax has to be repositioned, either through renovation, re-development or sale the nature of the financing that is available will have a short term time horizon meaning construction or bridge financing. Bill Wrench of *Phillips Realty Capital* broke down the capital markets and fair market debt assumptions as such.

In terms of construction and bridge financing there are four options:

1. Construction Permanent Lenders

2. Department of Housing and Urban Development (HUD)

3. Banks

4. Commercial Mortgage Backed Securities (CMBS)

There are very few construction permanent lenders in the market and those that are have not been as competitive as other lending sources on proceeds and interest rate. HUD offers financing for multi-family developments, however there is extensive lead time associated with this program. Therefore construction permanent lenders and the HUD program are not viable financing sources for 3701 N. Fairfax.

Today, Banks are the primary source of capital for deals of this nature. To ensure that the bank is protected in the event of default, banks require loans to be accompanied with a form of personal recourse, which burns down after the property is built/renovated and then goes away completely upon stabilization. Since, banks are also are in the business of holding deposits they generally require that the borrower further their relationship with the bank by holding a certain amount of money at said bank.

The CMBS markets were the most aggressive form of capital up until mid-2007. The downfall of the CMBS markets played in integral roll as the global economy went into recession. The CMBS markets have not resuscitated to the previous strength, but remain an option for borrowers. There are two common complaints with the CMBS markets, first the rate, proceeds and deal terms are not locked until the deal is complete. This creates uncertainty for borrowers, who need to make business decisions. Secondly, if a borrower's property goes into default, the special servicers who handle the assets from that point in time on are not responsive and difficult business associates.

Banks and CMBS have similar forms of underwriting properties given they both offer short term money. These lenders can attractively price that money, generally over the London Interbank Offered Rate (LIBOR), which was 0.24% as of March 4, 2012. The amount they price over the LIBOR is called a spread; spreads have been quoted at approximately 275 over Libor for similar deals to this structure. The money is charged on an interest only basis for the term of the loan, usually three years with a potential for one year extensions. Total proceeds fluctuate deal to deal and sponsor to sponsor, however a fair market rate is generally around 70% loan to cost (LTC). Debt yield (DY), defined as is (NOI / Loan Amount) is another common metric lenders use to determine proceeds, a 9.00% DY is market for well located properties with sponsors that have a proven track record.

Below are the underwriting assumptions *Luce Realty* has used in its highest and best use analysis for each use.

<u>Office Renovation</u>

LTC:	70%
Rate:	3.00% (approx 275 + LIBOR)
DY:	9.00%
Recourse:	Required

<u>Multi-Family Development</u>

LTC:	70%
Rate:	3.00% (approx 275 + LIBOR)
DY:	9.00%
Recourse:	Required

<u>Hotel Development</u>

LTC:	70%
Rate:	3.00% (approx 275 + LIBOR)
DY:	9.00%
Recourse:	Required

Office Renovation Analysis

FAR Analysis	
Site Size	56,010
FAR	3.25
Maxium Square Feet	182,033

Assumptions

Renovation Assumptions

Hard Costs	Price
Roof	500,000
Lobby	500,000
Elevators	1,000,000
Restrooms	500,000
HVAC	250,000
Exterior	750,000
Parking	250,000
Sitework	100,000
Demolition	300,000
Deferred Maintenance	250,000
Total Hard Costs	**4,400,000**
Soft Costs	
Permits & Fees	200,000
Contingency	400,000
Total Renovation Costs	**5,000,000**

Discounted Cash Flow Assumptions

Rental Assumptions	
Rental Rate / SF	$ 40.00
Expense Reimbursement	base stop
Parking per space	$125.00
Vacancy	8.00%
Expense Assumption	
Expense Rate / SF	$ 12.50

Renovation Costs

	Cost	Per SF
Land		
Existing Note	45,000,000	$ 247.21
Lease Up Cost		
Renovation Cost	5,000,000	$ 27.47
Tenant Improvements	8,646,544	$ 47.50
Leasing Commissions	2,600,000	$ 14.28
Contingency		
2%	1,224,931	$ 6.73
Financing Cost	1,311,901	$ 7.21
Total Cost	**63,783,376**	$ 350.40

Proforma

		Annual	Per SF
Income			
Base Rent	36.00	6,553,170	36.00
Expense Reimbursement		200,000	1.10
Parking (space per month)	125	227,541	1.25
Potential Gross Income		6,980,711	38.35
Vacancy	5%	(349,036)	(1.92)
Effective Gross Income		6,631,675	36.43
Expenses			
Total Per SF	12.50	2,275,406	12.50
Ratio	34.31%		
Net Operating Income		**4,356,269**	**23.93**
Return on Cost		*6.83%*	

JOHNS HOPKINS CAREY BUSINESS SCHOOL

Apartment Analysis

FAR Analyis	
Site Size	56,010
FAR	5.30
Maxium Square Feet	296,853
Core Area	10%
Net Rentable Square Feet	267,168
Average Unit Size	800
Units	334

Assumptions

Development Assumptions	Cost
Hard Costs	
Demolition	5,000,000
Site Work	2,500,000
Parking	2,500,000
Building	50,000,000
Hard Costs	
Percentage of Hard Costs	10%
Developers Fee	
Percentage of Hard Costs and Soft Cots	3%
Contingency	
Percentage of Hard Costs and Soft Cots	5%
Financing Cost	2,512,370

Proforma Assumptions	
Rental Assumptions	
Rental Rate (SF)	3.00
Premium Income	200,000
Parking (space per month)	125
Vacancy/Concessions	5.00%
Expense Assumption	
Expense per unit	10,000

Development Costs

		Cost	Per Unit
Land			
Existing Note		45,000,000	134,747
Hard Costs			
Demolition		$ 5,000,000	14,972
Site Work		2,500,000	7,486
Parking		2,500,000	7,486
Building		50,093,944	150,000
Total Hard Costs		60,093,944	179,944
Soft Costs			
of Hard Costs	15%	9,014,092	26,992
Developer Fee			
of Hard and Soft Costs	3%	2,073,241	6,208
Contingency			
of Hard and Soft Costs	5%	3,455,402	10,347
Financing Cost		2,512,370	7,523
Total Cost		**122,149,048**	**365,760**

Proforma

		Annual	Per Unit
Income			
Base Rent (SF per month)	3.00	9,618,944	28,803
Premium Income		200,000	599
Parking (space per month)	125	500,987	1,500
Potential Gross Income		10,319,931	30,902
Vacancy	5%	(515,997)	(1,545)
Effective Gross Income		9,803,935	29,357
Expenses			
Per Unit	10,000	3,339,911	10,001
Ratio	34.07%		
Net Operating Income		**6,464,023**	**19,356**
Return on Cost		*5.29%*	

Hotel Analysis

FAR Analysis			
Site Size	56,010	Net Rentable Square Feet	163,829
FAR	3.25	Average Rom Size	825
Maxium Square Feet	182,033	Keys	199
Core Area	10%		

Assumptions

Development Assumptions	
Hard Costs	Cost
Demolition	5,000,000
Site Work	2,500,000
Parking	2,500,000
Building	15,000,000
Hard Costs	
Percentage of Hard Costs	20%
Developers Fee	
Percentage of Hard Costs and Soft Cots	3%
Contingency	
Percentage of Hard Costs and Soft Cots	5%
Financing Cost	1,625,400

Proforma Assumptions	
Rental Assumptions	
Annual Occupancy	75%
Average Daily Rate	$168.00
Revenue Per Room	$125.66

*All other assumptions are based on market driven ratios as indicated by the below proforma.

Development Costs	Cost	Per Unit
Land		
Existing Note	45,000,000	226,608
Hard Costs		
Demolition	$ 5,000,000	25,179
Site Work	2,500,000	12,589
Parking	2,500,000	12,589
Building	15,000,000	150,000
Total Hard Costs	25,000,000	125,893
Soft Costs		
20%	5,000,000	25,179
of Hard Costs		
Developer Fee		
3%	900,000	4,532
of Hard and Soft Costs		
Contingency		
5%	1,500,000	7,554
of Hard and Soft Costs		
Financing Cost	1,625,400	8,185
Total Cost	**79,025,400**	**397,951**

Proforma	Annual	Per Key	Ratios*
Revenue			
Rooms	9,108,382	45,867	64.56%
Food & Beverage	4,500,000	22,661	31.90%
Premium	500,000	2,518	3.54%
Total Reveune	14,108,382	71,046	100.00%
Department Expenses			
Rooms	3,187,934	16,054	35.00%
Food & Beverate	3,510,000	17,675	78.00%
Other	375,000	1,888	75.00%
Total Department Expenses	7,072,934	35,617	50.13%
Profit	7,035,448	35,429	49.87%
Undistributed Expenses	3,809,263	19,182	27.00%
Gross Operating Profit	3,226,185	16,246	22.87%
Base Management Fee	423,251	2,131	3.00%
Fixed Expenses	634,877	3,197	4.50%
Net Operating Income	2,168,057	10,918	15.37%
FF&E Reserve	282,168	1,421	2.00%
NOI After Reserve	**1,885,889**	**9,497**	**13.37%**
Return on Cost	2.39%		

Return on Cost Table

Return on Cost by Use	
Office Renovation	6.83%
Multi-Family Development	5.29%
Hotel Development	2.39%

The above return on cost table gives a developer a high level overview of his potential development options. The first deduction is that the Hotel Development does not offer a developer enough yield to further purse this option. At a 2.39% return on cost, the debt required to build the structure (approximately 3.00%) is more expensive then the return resulting in negative leverage, meaning any debt you put on the property hinders your returns, henceforth we will write the hotel development option out as economically not viable.

Upon first look it seems that the Multi-Family development also does not offer enough yield (in today's market multi-family developers are looking for 7.00% return on cost) to merit a multi-family development. However, the cost of the existing note is creating a tremendous burden on the property. Given the nature of today's white hot multi-family market and location advantages of 3701 N. Fairfax, there may be a creative solution given the multi-family route, however the cost impediment of the note is significantly deteriorating exteriorizing the return on cost metric.

While examining the office renovation return on cost it is appears to be the most attractive option; however it is important to note that the office renovation does not include the additional hard costs of developing an entirely new building since the renovation costs are far less then the costs associated with demolition and developing a completely new building, its perceived return on cost is buoyed. Still if an appropriate budget can be formed, limiting cost over-runs with a aggressive leasing team in place the office renovation is a viable solution to the current predicament.

Sales Underwriting

Luce Realty has also considered the potential to sell the 3701 N. Fairfax. In order to establish a fair market value for the property Luce Realty has used the renovation budget, provided a conservative lease up schedule and used assumptions to create the discounted cash flow analysis contained herein.

Sales Assumptions

Renovation Assumptions

Hard Costs	Price
Roof	500,000
Lobby	500,000
Elevators	1,000,000
Restrooms	500,000
HVAC	250,000
Exterior	750,000
Parking	250,000
Sitework	100,000
Demolition	300,000
Deferred Maintenance	250,000
Total Hard Costs	**4,400,000**
Soft Costs	
Permits & Fees	200,000
Contingency	400,000
Total Renovation Costs	**5,000,000**

Discounted Cash Flow Assumptions

Rental Assumptions	
Rental Rate / SF	$ 40.00
Expense Reimb.	base stop
Parking per space	$ 125.00
Vacancy	8.00%
Expense Assumption	
Expense Rate / SF	12.50
Inflation	3.00%
Total SF	182,033

Renovation Costs

Lease Up Cost	Cost	Per SF
Renovation Cost	5,000,000	$ 27.47
Tenant Improvements	8,191,485	$ 45.00
Leasing Commissions	2,600,000	$ 14.28

Lease Up Schedule

	Date	SF
1st Floor	Jan-13	18,203
2nd Floor	Apr-13	18,203
3rd Floor	Jul-13	18,203
4th Floor	Oct-13	18,203
5th Floor	Jan-14	18,203
6th Floor	Jan-14	18,203
7th Floor	Apr-14	18,203
8th Floor	Jul-14	18,203
9th Floor	Oct-14	18,203
10th Floor	Dec-14	18,203

Residual Calculation		
Square Feet	182,000	
NOI	$ 7,136,022	in Year 10
Residual Cap Rate	7.0%	
Residual Value	$ 101,943,171	
Cost of Sale @ 2.0%	2,038,863.4	
Net Residual Value	$ 99,904,308	

Present Value Matrix

Yield	PV of CFs	PV of Resid.	Total PV	Value/SF	CFs as %	Resid. As %
9.00%	15,014,899	42,200,659	57,215,558	314.37	26%	74%
9.50%	14,369,149	40,312,806	54,681,955	300.45	26%	74%
10.00%	13,747,717	38,517,436	52,265,153	287.17	26%	74%
10.50%	13,149,551	36,809,629	49,959,179	274.50	26%	74%
11.00%	12,573,651	35,184,747	47,758,398	262.41	26%	74%

Given the present value for the property is approximately $52,266,000 *Luce Realty* is in a comfortable situation in which they could sell their building, pay off their existing loan and take a profit. Many owners in the real estate industry today are not afforded that luxury and will attempt to negotiate with the bank in hopes to have their loan written down. It is important to note that in the Washington, DC market, lenders have not been willing to write down loans on well located properties because the belief that the property will recoup its value quickly given the overall strength of the market.

Discounted Cash Flow Analysis
In Inflated Dollars for the Fiscal Year Beginning 1/1/2013

For the Years Ending	Year 1 Dec-2013	Year 2 Dec-2014	Year 3 Dec-2015	Year 4 Dec-2016	Year 5 Dec-2017	Year 6 Dec-2018	Year 7 Dec-2019	Year 8 Dec-2020	Year 9 Dec-2021	Year 10 Dec-2022
Potential Gross Revenue										
Base Rental Revenue	$7,281,200	$7,466,874	$7,638,381	$7,867,529	$8,103,555	$8,346,664	$8,588,622	$8,865,844	$9,125,102	$9,389,632
Absorption & Turnover Vacancy	(5,460,900)	(1,749,916)				(281,364)	(217,353)	(223,874)	(307,454)	
Scheduled Base Rental Revenue	1,820,300	5,716,958	7,638,381	7,867,529	8,103,555	8,065,300	8,371,269	8,641,970	8,817,648	9,389,632
Expense Reimbursement Revenue										
Total Expenses		139,828	336,692	397,522	460,178	413,521	395,423	342,036	299,761	368,303
Total Reimbursement Revenue	0	139828	336692	397522	460178	413521	395423	342036	299761	368303
Parking	154,500	309,000	309,000	309,000	309,000	309,000	309,000	309,000	309,000	309,000
Total Potential Gross Revenue	1,974,800	6,305,614	8,620,765	8,971,573	9,332,911	9,201,342	9,471,115	9,635,042	9,726,170	10,435,238
General Vacancy			(662,726)	(685,924)	(709,819)	(444,171)	(526,091)	(537,476)	(471,255)	(805,355)
Effective Gross Revenue	1,974,800	6,305,614	7,958,039	8,285,649	8,623,092	8,757,171	8,945,024	9,097,566	9,254,915	9,629,883
Operating Expenses										
Total Expenses	1,481,291	1,830,871	2,027,737	2,088,570	2,151,227	2,193,606	2,265,120	2,333,073	2,397,013	2,493,861
Total Operating Expenses	1,481,291	1,830,871	2,027,737	2,088,570	2,151,227	2,193,606	2,265,120	2,333,073	2,397,013	2,493,861
Net Operating Income	493,509	4,474,743	5,930,302	6,197,079	6,471,865	6,563,565	6,679,904	6,764,493	6,857,902	7,136,022
Leasing & Capital Costs										
Tenant Improvements	3,640,600	5,460,900				1,308,340	673,795	1,388,018	1,429,658	
Leasing Commissions	1,299,459	2,199,088				754,772	388,707	800,736	824,758	
Renovation Costs	5,000,000									
Total Leasing & Capital Costs	9,940,059	7,659,988	0	0	0	2,063,112	1,062,502	2,188,754	2,254,416	0
Cash Flow Before Debt Service & Taxes	($9,446,550)	($3,185,245)	$5,930,302	$6,197,079	$6,471,865	$4,500,453	$5,617,402	$4,575,739	$4,603,486	$7,136,022
	===========	===========	===========	===========	===========	===========	===========	===========	===========	===========
Capitalization Rate	7.00%									$ 101,943,171
Sales Proceeds Less Cost of Sale										$ 99,904,308
Cash Flow	($9,446,550)	($3,185,245)	$5,930,302	$6,197,079	$6,471,865	$4,500,453	$5,617,402	$4,575,739	$4,603,486	$ 107,040,330
NPV	$52,265,153									

As a culmination of the Financial Analysis *Luce Realty* believes it is important to outline some of the inherent risks with each potential use, before reaching a conclusion on its findings.

Market Risk: There is an unprecedented amount of uncertainty in the market today. Although, most financial analysts believe we have put the worst part of the financial crisis behind us, there is no definitive answer to what the future holds. Looming questions revolve around growth and de-leveraging our debt. Luce Realty would like to highlight some macro trends unearthed in the market feasibility section, which tie directly back into market risk.

In the office sector, tenants downsizing to become more efficient and tenants are vacating to accommodate BRAC. The Federal Governments mandate to be more efficient will also play a crucial role in the Washington Office Market. These factors place a tremendous amount of fundamental supply and demand uncertainty and market risk on the leasing front of an office renovation.

Construction Risk: The commodities markets have been turbulent and highly volatile over the last few years, which will dictate construction costs. Personnel, supplies and weather are just a few areas in which any number of issues could occur while developing a building causing cost overruns and pushing the development budget higher.

Approval/Permitting Risk: The fact that 3701 N. Fairfax is subject to site plan 46 further complicates the dynamics of a redevelopment for this site. It is anticipated that Arlington County will require certain proffers to help persuade Arlington County to approve the redevelopment. The proffers will be a net positive on the area, however they will be a costly venture for the developer. It is also anticipated that the developer will receive push back in a few hours and will need to hire a well respected and well compensated legal team to tackle some of these issues.

Luce Realty is faced with a pending capital event forcing a decision to be made on its 3701 N. Fairfax asset. As discussed previously the hotel option does not offer attractive returns. Likewise, the multi-family development, although intriguing from a long term sentiment does not offer the returns a developer would expect from a comparable project. The last development option is an office building renovation, which for all reasonable purposes should be viewed as a speculative office building, given there are no tenants lined up to absorb the building, accompanied by the long term trends the office feasibility analysis revealed *Luce Realty* does not believe the returns garner further pursuit of this option. This leaves the last option, the sale of 3701 N. Fairfax, an option that solves all the questions revolving around the capital event, while producing a sizable profit. The proceeds used from the sale, would ultimately be used to payoff the existing note on 3701 N. Fairfax, with additional profits available to finance future real estate projects.

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