

# APPRAISAL REPORT

Ground Rental Rate Analysis  
Involving the Salem Airport  
(McNary Field – SLE)  
Salem, Oregon



Valuation Date	February 2, 2015
Prepared For	Clint Dameron Real Property Services Manager Urban Development Department City of Salem
Prepared By	William E. Adams, MAI
File No.	141201

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February 24, 2015

Mr. Clint Dameron  
Real Estate Services Manager  
City of Salem  
350 Commercial Street NE  
Salem, Oregon 97301

RE: Appraisal Assignment - Ground Rental Rate Analysis Involving the  
Salem Airport (McNary Field) in Salem

Dear Mr. Dameron:

At your request, I have prepared a real estate appraisal estimating the ground rental rate for land within the boundaries of the Salem Airport (McNary Field). The City of Salem owns the land within the airport's boundaries. The City has segregated the airport into six areas (subzones). Historically, the City has charged different ground rental rates to tenancy in these subzones. The City is now negotiating leases under a revised lease agreement and the same ground rental rate will be charged for new tenancy regardless of their location within the airport.

As the parcels within the airport's boundary vary in attributes such as size, vehicle access, utility availability, and access to taxiways, a set of attributes needed to be determined for this appraisal assignment. Therefore, by mutual agreement between the appraiser and the client, this appraisal assignment estimates the annual ground rental rate for a typical lot, with the typical lot attributes & entitlements identified as follows. Specifically, the typical lot has available municipal utilities, a parcel size between 15,000 SF and 1 acre (43,560 SF), a utilitarian shape, aircraft taxiway access, available vehicle access (either gated or unrestricted from public roadway), and the underlying land is zoned I-P.

The annual ground rental rate for the typical lot is estimated as of February 2, 2015, coinciding with the most-recent property inspection. The interest appraised is the fee simple estate. The intended use of this appraisal is to assist the client (City of Salem) in their establishment of a rental rate for land leases and renewals within the Salem Airport. The intended user of this report is limited to the client. The use of this appraisal by anyone other than the stated intended user, or for any use than the stated intended use, is prohibited.

This report is prepared in compliance with the current Uniform Standards of Professional Appraisal Practice (USPAP), as formulated by The Appraisal Foundation as well as the Standards of Professional Appraisal Practice and the Code of Professional Ethics of the Appraisal Institute.

Mr. Clint Dameron  
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The appraisal is prepared in accordance with USPAP Standards Rule 2-2(a) for an appraisal report. The scope of work utilized for this assignment is considered typical for this property type, the proposed transaction, and the intended use. The report format is consistent with the summary report format from the 2012 USPAP guidelines.

The appraiser has sufficient education and experience in valuing similar properties to satisfy the competency rule of the Uniform Standards. The reported lease rate is not based on a requested rate and the appraiser was acting independently of the client during the course of this assignment.

Reference to the Assumptions and Limiting Conditions section of the attached report is recommended for a complete understanding of the basis on which the value of the subject property is predicated. At the client's direction, the following hypothetical condition and extraordinary assumption (as defined by USPAP) are employed.

*This appraisal assignment does not estimate a ground rental rate for a particular parcel of property within the Salem Airport. Rather, the ground rental rate estimate applies to a "typical lot" within the airport that has specified land attributes and entitlements. For the purpose of this assignment, the typical lot has available municipal utilities, a parcel size between 15,000 SF and 1 acre (43,560 SF), a utilitarian shape, aircraft taxiway access, available vehicle access (either gated or unrestricted from public roadway), and the underlying land is zoned I-P. The preceding lot attributes are recognized as a hypothetical condition for this assignment.*

*The appraiser was provided with a sample lease agreement to be used for new ground leases negotiated within the boundaries of the Salem Airport. This appraisal is predicated on the extraordinary assumption that the lease terms to be negotiated for land leases and renewals will significantly conform to the lease terms cited in the provided lease agreement. The appraiser notes that certain departures from the provided lease agreement may impact the ground rental rate estimated for the typical lot.*

After considering all of the data assembled for this appraisal assignment, the ground rental rate for a typical lot within the Salem Airport boundaries as of the February 2, 2015 valuation date is estimated to be:

**\$0.34/SF Annually on a Triple Net (NNN) Expense Basis**

The preceding ground rental rate is dependent upon the stated extraordinary assumption and hypothetical condition. The reasoning and analysis leading to this conclusion are discussed in the following appraisal report.

Respectfully Submitted,



William E. Adams, MAI

Corporate bonds. Corporate bonds require a premium return over Treasury bonds due to the higher risk; however, the liquidity differences between these investments and ground leases result in a spread of return rates that do not aid this analysis.

The appraiser also surveyed numerous airports in this region as to their ground leasing activity and if annual return rates are utilized in their lease calculations or negotiations. Certain airports market leased space based on lease rates surveyed from other area airports. Conversely, other airports negotiate leases based on an annual return rate applied to the land value. Some airports specify a 10 percent return rate and lessees can "take it or leave it" while other airports anticipate a 10 percent return rate, but then negotiations may result in a lower accepted return rate. Still other airports will justify the lower rates (below the 10 percent asking rate) due to their fee structure which allows the airport to charge certain additional fees to lessees. The Port of Portland utilizes a 10 percent return rate at its Hillsboro and Troutdale Airports while the City of Corvallis uses a similar methodology for the Corvallis Airport.

Based on the data assembled for this analysis and considering the attributes of the typical lot within the Salem Airport, an annual rental return rate of 8.5 percent is estimated for this ground rent analysis.

Applying an 8.5 percent annual return rate to the \$4.00/SF land value estimated for a typical lot within the Salem Airport results in a total annual ground rental rate of \$0.34/SF NNN.

## AIRPORT GROUND LEASE SURVEY ANALYSIS

An alternative method to deriving an annual ground rental rate applicable to land within the Salem Airport involves surveying other airports in the region and analyzing annual ground rental rates charged at these airports. For this survey, information was obtained from six airports in the greater Portland Area and the Willamette Valley. Interviews were conducted with either airport managers or staff handling leasing duties for the respective airports. It is noted that some consistency is evident for all airport ground leases. All surveyed airports charge ground rents on a triple net (NNN) basis whereby the lessee is responsible for all ownership and operating expenses associated with the leased site. Certain airports require the lessee to pay property taxes despite the airport being under a tax-exempt ownership. Lease durations tend to be for 20 to 30 years with one or more lease renewal options. The only exception is the Eugene Airport where their leases are typically structured on a 10-year duration with a 10-year renewal option. Longer leases can be negotiated but a large share of the land leases at the Eugene Airport are situated under relatively old hanger buildings; thus, the shorter lease duration is reasonable. For new construction subject to a ground lease, a longer duration can be negotiated at this airport.

Airports periodically obtain appraisals to establish annual ground rental rates on a 3 to 5 year basis, with annual rent adjustments via CPI being most common. The only exception involves the Eugene Airport where specific step-up rent adjustments are employed.

With regard to the land area subject to the ground lease, most airports base the lease rate on a specific site area, with most airports willing to meet the lessee's site requirements for structures, vehicle parking, aircraft ramps, open storage, etc. Certain leases involving condominium hangers, t-hangers, or old structures may be based on a building footprint

plus a surrounding setback from the building, but the majority of leases involve a leased site with sufficient area for site & building improvements as well as aircraft ramps.

Most of the airports surveyed for this assignment indicate that they have an available land inventory for new ground leases. The Aurora Airport cites that only approximately four acres of land is available for new ground lease activity, with multiple prospective tenants vying for this land. The airport representative indicates that he expects the airport to have all its available land area absorbed by this summer. The McMinnville Airport is reported to have between 10 and 15 acres available for new ground lease while the remaining four airports cite that a significant amount of land is available. Three of the airports have in excess of 100 available acres, while the Corvallis Airport reports between 1,200 and 1,300 acres available. All of this land inventory is within the airport fence-line and is accessible to aircraft. Some of the airports have additional land under their authority that is outside the fence-line and does not allow aircraft access; however, such land activity is not discussed for this assignment as the subject's typical lot being appraised is assumed to be within the fence-line.

Regarding current demand for the available land inventory, most airports surveyed for this assignment have witnessed increased ground lease activity during the past few years. For a few years after the recession, ground lease activity at most airports was minimal. As the economy has improved and financing alternatives have increased, demand for land for airport-oriented use has grown. It is noted that recent lease activity at various airports involves both general aviation and commercial users (all within the fence-line).

Airport personnel were also interviewed regarding the impact of specific site attributes and their influence on the asking or negotiated ground rents. Such factors that were discussed include variance in site size, the site's vehicular access being unrestricted or via a secured/gated access point, the level of utility services available to a site, differences in zoning designations & allowable uses, and any building height restrictions imposed by FAR Part 77 regulations that would impact the development potential or size of the building footprint within certain lots. All sites within the fence-line have aircraft access to taxiways & runways.

The following paragraphs discuss each of the surveyed airports. Additional airport information not relevant to this discussion & analysis are retained in the appraiser's work file.

The **Aurora State Airport (UAO)** is a Category 2 airport operated by the State of Oregon. This airport is situated north of Salem along the east side of the Interstate 5 corridor in north Marion County. This airport is a general aviation airport with no tower, multiple FBOs, and one 5,004-foot runway. John Wilson (State Airport Operations Specialist) indicates that the year-2015 ground lease rate for land at this airport is **\$0.29/SF NNN annually**. Despite state ownership, lessees pay property taxes on their leased site. Lease rates are based on appraisals conducted every 5 years, with interim rental rate increases on two-year cycles based on the CPI. The leased site is determined based on the lessee's site requirements which may include a ramp. Certain users only require a hanger abutting a taxiway. In those circumstances, the leased site is calculated as the building footprint plus a surrounding 5-foot setback. However, most leases involve site areas. Leases are typically negotiated on a 25-year term plus a 5-year renewal option. According to Mr. Wilson, demand at the airport has significantly improved. Only 4 acres of developable land remains and one party has

shown interest in leasing the entire site with multiple parties also showing interest in leasing portions of this remaining site area. Both lease renewals and new leases are occurring at the airport. There are many older leases that are expiring and being brought up to market rent. Demand is present for both small and large site users. All sites within the fence-line of this airport have similar aircraft & vehicle accessibility, available utilities, building height restrictions, and zoning designation. No adjustment to the rental rate is made for differences in site size. This airport has 446 resident aircraft and witnessed 260 daily flight operations.

The **Corvallis Airport (CVO)** is a Category 2 airport operated by the City of Corvallis. This airport is situated just south of the Corvallis city limits near Highway 99. This airport is a general aviation airport with no tower, one FBO, and two runways (5,900 & 3,545 feet). Don Mason (Airport Manager) indicates that the airport manages land both within the fence-line and in an industrial park adjacent to the airport but lacking aircraft access. The current ground rental rate for land within the fence-line is **slightly less than \$0.25/SF NNN annually**, with the rent adjusting upward via CPI in May. The lease rate is established based on a 10 percent annual return of the land value (based on appraisals). Appraisals are conducted every 5 years with interim rental rate increases based on an annual CPI adjustment. The new lease rate is based on an appraisal prepared in January 2011. A new appraisal will be completed for 2016. The specified lease duration is 20 years with two 10-year renewal options. The majority of leases are based on the site area and not the building footprint plus setback method. Only some t-hangers owned by the City have ground leases based on the latter method as these hangers have no areas devoted to site improvements or ramps.

The most recent lease negotiated at the Corvallis Airport occurred in 2014. The tenant has built other hangers at the airport, with this new lease representing a 7,680 SF site (with ramp) at an annual lease rate of \$0.251/SF NNN. The lease has a 20-year lease term plus two 10-renewal options. This rent is scheduled to adjust via CPI in May 2015. All existing City-owned hangers at this airport are nearly 100 percent occupied. Currently, two hangers are vacant, but multiple prospective tenants have shown interest in leasing the hangers. The Corvallis Airport has between 1,200 and 1,300 acres available within the fence-line for new development. All sites within the fence-line of this airport have similar aircraft & vehicle accessibility, available utilities, building height restrictions, and zoning designation. No adjustment to the rental rate is made for differences in site size. This airport has 162 resident aircraft and witnessed 143 daily flight operations.

The **McMinnville Airport (MMV)** is a category 2 airport located in south McMinnville near State Highway 18. This airport is operated by the City of McMinnville. This airport is a general aviation airport with no tower, one FBO, and two runways (5,420 & 4,676 feet). Graham Goad (Airport Manager) indicates that the current ground lease rate for land at this airport is **\$0.245/SF NNN annually**. Lease rates are based on appraisals conducted at periodic intervals, with annual rental rate increases via a CPI adjustment. Evergreen Aviation was a large tenant at the airport and their recent bankruptcy has left many hangers and offices vacant. Erickson Helicopters bought Evergreen Helicopters and now operates out of a new hanger originally built for Evergreen. While there has been some interest by prospective tenants for land at this airport, the Airport Manager indicates that the 35-year minimum lease term (with no renewal options) is hindering lease negotiations. No new land leases have been negotiated at this airport since July 2010. At this airport, the leased area is calculated using the building footprint plus setback method. However, the majority of leases

are structured using a site area (including ramps and outside storage). All sites at the airport have similar attributes in terms of aircraft & vehicle accessibility, available utilities, building height restrictions, and zoning designation. No adjustment to the rental rate is made for differences in site size. The airport has between 10 and 15 acres available for ground lease and new development. This airport has 126 resident aircraft and witnessed 174 daily flight operations.

The Port of Portland manages both the Hillsboro Airport and the Troutdale Airport. Isaac Barrow (Senior Leasing Agent) was interviewed regarding the attributes of both airports.

The **Hillsboro Airport (HIO)** is a category 2 airport located in Portland's Sunset Corridor. This airport is a general aviation airport with significant corporate aircraft activity. This airport has a tower, multiple FBOs, and two runways (6,600 & 4,049 feet). The airport contains land within the airport's fence-line as well as land abutting the airport but suitable for general industrial or commercial use. Some of the airport land is currently occupied by a shopping center. The Airport Authority (Port of Portland) just bought (in December 2014) 47 acres for \$4.25/SF and intends to integrate part of the newly-acquired site within the Airport's fence-line, with the balance adjoining the fence-line. Mr. Barrow indicates that the current ground lease rate for land within the airport's fence-line is **\$0.40/SF NNN annually**. It is noted that lessees also pay property taxes on their leased site. Lease rates are based on appraisals performed every 3 years, with annual rental rate increases via a CPI adjustment. An annual rental return rate of 10 percent is used for these leases. Demand for sites within the airport has improved; with two FBOs expanding facilities and a new lease to a third tenant being negotiated in December 2014 at the \$0.40/SF annual rent level. This lease covers approximately 4 acres on a 30-year lease term with the buyer intending to build a hanger for a new FBO. A few condominium hanger sites are available and their leased area is calculated using the building footprint plus setback method. However, the majority of leases are structured using a site area. Leases are typically negotiated on a 20 to 30-year term, but some leases have been structured on a 40-year term.

The Hillsboro Airport currently has approximately 150 acres available for lease within the fence-line. All sites at the airport have similar attributes in terms of available utilities and zoning designation. No adjustment to the rental rate is made for differences in site size. Some sites have secured vehicular access while other sites allow unrestricted access via public roadways. Also, some sites have low allowable building heights due to FAR Part 77 restrictions. However, the airport charges a similar ground rental rate despite these differences in access or allowable building height. This airport has 265 resident aircraft and witnessed 695 daily flight operations.

The **Troutdale Airport (TTD)** is a category 2 airport located in Troutdale east of Portland. This airport also lies on the approach of the Portland International Airport (PDX) and its location has hindered some air traffic & development activity. This airport is in the process of a Master Plan review, with Mr. Barrow citing that the FAA would like to lessen the activity at this airport due to its proximity to PDX. This airport no longer caters to many commercial tenants, but remains popular for recreational pilots. This airport is a general aviation airport with a tower, one FBO, and one 5,400-foot runway. The airport contains land within the airport's fence-line as well as commercial land abutting the airport and in proximity to highway service and truck-stop uses. Mr. Barrow indicates that the current ground lease rate for land within the airport's fence-line is **\$0.28/SF NNN annually**.

Lessees also pay property taxes on their leased site. Lease rates are based on appraisals performed every 3 years, with annual rental rate increases via a CPI adjustment. An annual rental return rate of 10 percent is used for these leases. Sites are leased at this airport based on a specified site area needed by the lessee. Only a few older existing leases calculate the site area using the building footprint plus setback method. Leases are typically negotiated on a 20 to 30-year term. While some lease renewals have occurred, this airport has not negotiated a new ground lease in over 10 years. Mr. Barrow indicates that interest in new site development within the airport's fence-line is essentially nil. The airport currently has approximately 100 acres available for lease within the fence-line. All sites at the airport have similar attributes in terms of available utilities and zoning designation. No adjustment to the rental rate is made for differences in site size. Some sites have secured vehicular access while other sites allow unrestricted access via public roadways. Also, some sites have low allowable building heights due to FAR Part 77 restrictions. However, the airport charges a similar ground rental rate despite these differences in access or allowable building height. This airport has 134 resident aircraft and witnessed 288 daily flight operations.

**Eugene's Mahlon Sweet Airport (EUG)** is a category 1 airport located northwest of the Eugene city limits. This airport offers regularly-scheduled commercial service by multiple regional & national airlines. This airport is tower-controlled, has one FBO, and two runways (8,009 & 6,000 feet). The airport contains land within the airport's fence-line suitable for general aviation as well as commercial-carrier use. Ms. Kathy Nasholm (Airport Administration) indicates that the current ground lease rate for land within the airport's fence-line is **\$0.32/SF NNN annually** for general aviation use and \$0.34/SF NNN annually for commercial-carrier use. Lease rates are based on appraisals performed every 3 years, with the appraisals also specifying specific step-up rates to be used for annual rent adjustments. The airport contains approximately 100 acres of land within the fence-line suitable for new construction. The majority of existing ground lease tenancy have sites developed with old hangars. As such, the airport calculates the leased site area using the building footprint plus setback method; however, they implement a site area methodology for new development on bare land.

Leases within the Eugene Airport are negotiated on a 10-year term plus a 10-year renewal option. According to Ms. Nasholm, demand for leased sites within the airport's fence-line has improved significantly during the past few years. Multiple ground leases were negotiated in 2014 and two leases are currently pending approval. Leased area varies, but most leased areas are less than one acre. Aside from new leases, a number of lease renewals have occurred. All sites within the airport's fence-line have similar attributes in terms of building height restrictions and zoning designation. No adjustment to the rental rate is made for differences in site size, gated versus unrestricted site access, or the level of available utilities. This airport has 185 resident aircraft and witnessed 166 daily flight operations.

Overall, airports within this region charge annual ground rental rates between \$0.245 and \$0.40/SF NNN. Tenancy at the Aurora, Troutdale, and Hillsboro Airports pay property taxes on their leased site, while lessees at the other municipal airports (including the Salem Airport) do not pay property taxes. Locational factors, airport features, level of services, and the number of resident aircraft appear to influence the rental rates charged at these various airports. Arraying the number of daily aircraft operations at each airport reveals no correlation between airport activity and rental rates; however, it is noted that Hillsboro's



daily aircraft operations (695) significantly exceeds the other airports surveyed and has the highest annual ground rent (\$0.40/SF NNN).

The Salem Airport has a reported count of 182 resident aircraft. Slightly lower counts are witnessed by the Corvallis (162) and Troutdale (134) airports with their annual ground rent being slightly less than \$0.25/SF (Corvallis) and \$0.28/SF (Troutdale). Two airports that are bracketed higher than the Salem Airport include the Eugene Airport (185) at \$0.32/SF and Hillsboro (265) at \$0.40/SF. It is noted that resident aircraft counts is not a primary factor for consideration in this analysis; yet it reflects some level of local demand attributes. It is further recognized that the high and low counts are represented by the McMinnville Airport (126) and the Aurora Airport (446), with their respective annual ground rental rates being \$0.245 and \$0.29/SF.

With regard to control tower presence, the three airports lacking a control tower (Aurora, Corvallis, & McMinnville) generate annual ground rents in the lower end of the range (between \$0.245 and \$0.29/SF NNN). Conversely, the three airports with an active control tower (Hillsboro, Troutdale, & Eugene) generate generally higher annual ground rents between \$0.28 and \$0.40/SF NNN.

Regarding locational and other factors, the annual rental rates at the Aurora, Corvallis, McMinnville, and Troutdale Airports require upward adjustment suggesting that the subject's annual ground rental rate is greater than \$0.245 to \$0.29/SF NNN. Despite the Eugene Airport offering commercial air service as well as general aviation service, the \$0.32/SF NNN annual rental rate being charged at this airport requires a slight upward adjustment for comparison with the Salem Airport. Conversely, the Hillsboro Airport has superior attributes to the Salem Airport and a downward adjustment to the \$0.40/SF NNN annual ground rental rate is appropriate. .

Overall, the survey of other area airports suggests that the annual ground rental rate for a typical lot at the Salem Airport is slightly greater than \$0.32/SF NNN and less than \$0.40/SF NNN. This range supports the \$0.34/SF NNN annual ground rental rate using the land value x annual ground rental return rate method previously estimated for this assignment.