

Preservation and Community Management Strategies Technical Report

To: Leasehold Feasibility Working Group

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Re: DRAFT Report on Preservation and Community Management Strategies at Fort Monroe

Date: June 24, 2011

Background

The 2007 General Assembly passed enabling legislation (2007 HB3180) that contemplated property conveyance at Fort Monroe to private parties provided it was consistent with the Reuse Plan: *“As to real property or interests therein owned or held in whole or in part by the Authority, whether acquired by reverter of title, purchase, gift, condemnation, or otherwise, no such real property or ownership interests in the former federal area known as Fort Monroe shall be subject to any land use, zoning, or subdivision ordinance of any city so long as such real property or interests therein are owned or held by the Authority. However, the conveyance of any interest in the real property from the Authority to a private party shall be consistent with Fort Monroe's reuse plan and contingent upon the private party's obtaining all necessary approvals under applicable land use law or ordinance.”* [2007 § 15.2-6304.1(D)].

In 2008, the concept of the leasing-only strategy was introduced by the Fort Monroe Federal Area Redevelopment Authority (FMFADA) as a means to provide a higher level of protection and control while providing the financial resources to sustain the historic properties. This strategy was incorporated by the 2010 General Assembly in the Fort Monroe Authority Act by passage of HB1297 that states: *“It is the policy of the Commonwealth that property at Fort Monroe shall not be sold to private interests, but shall be maintained as Commonwealth-owned land that is leased, whether by short-term operating/revenue lease or long-term ground lease, to appropriate public, private, or joint venture entities. If the decision is ever made to sell property at Fort Monroe, it may only be sold with the consent of both the Governor and the General Assembly, and approval as to form of the documents by the Attorney General”* [2010 § 15.2-7304(A)].

The new Fort Monroe Authority (FMA) Board of Trustees established by HB1297 began to revisit some of the decisions made by the FMFADA Board including the lease-only strategy. Several of the FMA Trustees openly expressed concern about the sustainability of the economic model and the decision to

pursue prepaid leaseholds as a financing mechanism for implementing the capital improvement plan. Similar concerns have been expressed by representatives of the Hampton City Manager's office and members of the U.S. Army Deputy Assistant Secretary of Installations and Housing office negotiating the Economic Development Conveyance with the FMA.

The 2011 session of the General Assembly passed SB1400 which moderated the conveyance language to read: *"It is the policy of the Commonwealth that the historic, cultural, and natural resources of Fort Monroe be protected in any conveyance or alienation of real property interests by the Authority. Real property in the Area of Operation at Fort Monroe may be maintained as Commonwealth-owned land that is leased, whether by short-term operating/revenue lease or long-term ground lease, to appropriate public, private, or joint venture entities, with such historic, cultural, and natural resources being protected in any such lease, to be approved as to form by the Attorney General of the Commonwealth of Virginia. If sold as provided in this article, real property interests in the Area of Operation at Fort Monroe may only be sold under covenants, historic conservation easements, or other appropriate legal restrictions approved as to form by the Attorney General that protect these historic and natural resources and only with the consent of both the Governor and the General Assembly, except that any transfer to the National Park Service shall require only the approval of the Governor."* [2011 § 2.2-2340(A)]

The FMA Board commissioned a study to investigate the feasibility of the prepaid leasing concept in the Hampton Roads market including the ability to obtain mortgage financing on prepaid leasehold interests and the marketability of leasehold interests to potential leaseholders in the area. The report was prepared by Bay Area Economics (BAE) and presented to the FMA Board of Trustees on March 24, 2011. The final version of the BAE Technical Memorandum dated April 13, 2011 contains the following conclusions:

- *A Prepaid Residential Leasehold program presents the FMA with a sub-optimal business proposition: lower sales revenues with higher costs both in terms of staff time and out-of-pocket expenses than would likely be the case with a fee-simple sales program.*
- *The FMA should consider adopting a fee simple sales program with property controls implemented through deed restrictions; Covenants, Conditions and Restrictions documents (CC&Rs); and historic preservation easements/covenants as set forth in the Programmatic Agreement – the degree of control would be virtually equivalent to that achieved under a leasehold structure since the Programmatic Agreement and its mandated controls apply to both forms of ownership.*

The Leasehold Feasibility Working Group (LFWG) was established to continue the evaluation of the prepaid leasehold financing strategy currently based on the BAE technical report on prepaid leasehold feasibility prepared by BAE Principal David Shiver. The FMA Board has requested a recommendation from the LFWG on the merits and feasibility of prepaid leasehold interests versus fee simple sales.

At its organizational meeting on April 26th, the LFWG group discussed the prepaid leasehold program and its impact on the economic model. The current version of the economic model reflects prepaid leasehold financing on the 174 family housing units only. The Monroe Apartments are expected to be operated by

the FMA as short-term rental housing. The commercial buildings are expected to be leased through either short-term operating leases or long-term leaseholds to provide operating funds for the Fort Monroe Authority. Since commercial financing is available for commercial properties leased through long-term leasehold agreements, the focus of this report is limited to the 174 family housing units, an inventory of which is attached as Exhibit A.

The LFWG identified four possible revenue generating strategies for the family housing units:

1. Rental income from short-term operating leases,
2. Rental income from long-term leasehold interests with no prepayment,
3. Rental income from long-term leasehold interests with prepayment of rent through mortgage financing, and
4. Fee simple sales to private individuals or investors.

This sub-group was tasked with investigating whether the existing leasehold strategy would provide a higher level of protection than fee simple sales with deed restrictions or historic easements. The sub-group met on May 24th to evaluate the protection mechanisms currently in place or foreseen that could be put in place to protect the 174 historic housing units and to manage the property in any of the four scenarios. During the meeting the Virginia Department of Historic Resources (DHR) reminded the group that the other side of this analysis is the economics. The DHR stated its belief that preservation and prosperity go hand and hand and recognize that what creates a sustainable economic picture also works best for the historic resources.

It should be noted that the prepaid leasehold strategy was projected to generate approximately \$37 million to be used to fund the capital improvement plan. If the prepaid leasehold strategy is not pursued by the FMA, alternative sources of capital funds must be identified and procured to fund the necessary infrastructure and utility upgrades.

For that reason this report will cover the protection mechanisms available to the FMA for historic assets and management of the property as a community as well as the impact of the four conveyance strategies on the economic sustainability and capital improvement plan of Fort Monroe.

Preservation and Community Management Tools

The following list identifies the range of tools already in place or foreseen in accordance with governing documents to address preservation and those identified as available for the management of the community at Fort Monroe, together with a brief description of each tool.

- Programmatic Agreement – In order to provide a framework for future stewardship and protection of historic properties at Fort Monroe, including individual buildings and structures, archaeological sites, landscape features, and historic viewsheds, as well as the National Historic Landmark (NHL) district as a whole, a Programmatic Agreement (PA) was executed in 2009.

The PA is a legally enforceable document that binds the signatory parties to its terms, and certain

roles and responsibilities. It provides a holistic approach to the long-term protection of culturally significant resources on the entire 565-acre property at Fort Monroe while also recognizing that different areas or zones have their own distinctive character and quality. The stipulations and tools called for in the PA are interconnected in order to provide a system of checks and balances to ensure consistency with preservation intent. Additionally, the PA provisions were written to anticipate a range of uses or change in property ownership, management or control, whether through subsequent delegation, lease, sale or other conveyance.

For instance, the stipulations require that parties not bound by the PA directly as signatories shall be bound through available legal and appropriate mechanisms. These might include, for example, management agreements with delegated parties, incorporation of the relevant terms of the PA into any lease, the use of perpetual easements in the case of the sale of property or timed covenants in the case of long term conveyances. Moreover, the PA's overarching framework for stewardship can and should be complemented by other tools to address neighborhood issues normally managed through CC&Rs or local zoning, for example.

The PA focus is on the physical treatment of historic, architectural, archaeological, and landscape features. The treatments are grounded in accepted best preservation practices and are informed by the National Park Service (NPS) guidance found in *The Secretary of the Interior's Standards for the Treatment of Historic Properties* and other NPS reference materials as these may be amended in the future. Interconnected tools employed in the PA to ensure proper treatment of historic properties include a Management Zone concept and the use of a Historic Preservation Manual and Design Standards (Design Standards) at the operational level. (The Standards must be approved by NPS and DHR.) These requirements are further supported by the critical and defined role of a professionally qualified Fort Monroe Historic Preservation Officer and the continuing review of all projects by the State Historic Preservation Officer.

The PA delineates seven areas called "Management Zones" based on their distinctive architectural character, land use, density and other factors. The PA also sets forth broad guidelines specific to each zone and its character, to include allowable new construction, limits to demolition and preservation treatments. The Design Standards take these guidelines and provide a detailed breakout of what is acceptable by zone and subzone. In this way, the Standards lay out specific guidelines for historic preservation treatments and design acceptable characteristics for new and infill construction and additions, including architectural style, massing, scale, materials, site placement, etc. The PA mandates that projects affecting historic buildings, structures and landscapes and any new development shall be reviewed and approved on the basis of consistency with the zone management treatment principles and the detailed Design Standards. Other projects may be considered only after all efforts are made to avoid or minimize adverse effects. Such projects must also be fully justified by data that supports that there is no feasible or prudent alternative.

Requirements of the PA that bind signatories to protect historic properties

Below is a list of PA stipulations that bind signatory parties to the perpetual protection of historic properties at Fort Monroe regardless of ownership, lease arrangement or controlling interest in

those properties:

- Stipulation I.F.3: This stipulation requires the Army, prior to the sale, transfer or lease of land that will not revert to the Commonwealth to develop in consultation with the other signatory parties “model historic preservation covenants, easements or other appropriate protections to be attached to the deed or lease agreements.” The stipulation also requires that the Army, immediately prior to transfer, record the finalized covenants, easements or other appropriate protections with the City of Hampton conveyance records, or attach these protections to the lease which shall be similarly recorded. The Army is forbidden to “transfer property out of Federal ownership or control without adequate and legally enforceable restrictions or conditions to ensure that the long-term preservation of the property’s historic significance.”
- Stipulation II.F: This stipulation commits the Commonwealth and the Fort Monroe Authority (as successor in interest my law to the Fort Monroe Federal Area Development Authority, to continuing enforcement of the terms of the PA related to matters of preserving and protecting the historic properties at Fort Monroe. As stated in the PA this is to be accomplished by the Commonwealth and FMA “in the event of transfer of any interest in the real estate or delegation of their interest in, or respective responsibilities for, Fort Monroe” by binding the transferee or the delegate “to the terms of this Agreement [i.e. the PA] as appropriate through available legally enforceable mechanisms.” Such “legally enforceable mechanisms” may include, but are not limited to, historic preservation easements held by DHR and/or a historic zoning ordinance established by the City of Hampton.
- Stipulation IV.C.6(i): According to this stipulation the Commonwealth must, in consultation with DHR, develop criteria that shall guide the decision-making process for the sale, transfer or lease of historic properties at Fort Monroe. The purpose of this requirement is to ensure that the implications to an historic property being removed from Commonwealth ownership or control are taken into consideration and carefully addressed. Among those items that must be included in this criteria are an economic analysis comparing retention of the historic property under Commonwealth ownership and control versus the sale, transfer or lease of the property to another entity, anticipated effects to the characteristics that make the historic property eligible for the National Register of Historic Places (NRHP) individually or as a contributing resource within the NHL historic district, the historic significance of the property, the physical condition of the property, and an evaluation of the feasibility and practicality of mothballing the historic property until the Commonwealth can identify a future use for the property.
- Stipulation IV.C.6(ii): As with the Army requirement found in Stipulation I.F.3, the Commonwealth, in consultation with DHR, must also develop “historic preservation covenants, easements or other appropriate protections to be attached to the deed or lease agreements” of historic properties leaving Commonwealth ownership or control. Additionally, such protections must be consistent with the established principles of the PA.
- Stipulation IV.C.6(vi): This stipulation states that the Commonwealth, prior to transfer of property to a party not bound by the PA, it “shall take such necessary steps to ensure that the protections afforded by the [PA] are enforceable against such party by the Commonwealth, the [FMA], the City of Hampton, or such entity as may have jurisdiction over the property at the time through local zoning and/or other appropriate tools.” The purpose of this stipulation is to ensure the continued protection of historic properties at Fort Monroe even in the event

that such properties are acquired, through lease or sale, by an entity that is not subject to the terms of the PA.

Requirements of the PA for the treatment of historic properties

Below is a list of PA stipulations that address the treatment of historic properties at Fort Monroe by signatory parties or other controlling interests:

- Stipulation II.E: In the event that the NPS acquires some or all of Fort Monroe as a National Park, the federal agency is responsible for compliance with Section 106 and Section 110 of the National Historic Preservation Act.
- Stipulation III.A: The FMA shall develop a Historic Preservation Manual and Design Standards (Design Standards) for activities occurring on the reversionary and non-reversionary lands at Fort Monroe. The Design Standards shall be “consistent with sound and accepted preservation practices and standards” and shall be informed by NPS publications and guidance documents such as *The Secretary of the Interior’s Standards for the Treatment of Historic Properties*, its Preservation Briefs and Tech Notes, as well as other appropriate sources. The Design Standards will, at a minimum, include the array of treatment options (rehabilitation, restoration, reconstruction, and preservation), address routine maintenance and repair activities, establish parameters for appropriate design (e.g. massing, scale, materials, locations, etc.) within each zone of the NHL historic district, respect the identified historic landscapes and significant viewsheds, and assess the potential to affect archaeological sites. The Design Standards must be reviewed and approved by DHR and NPS and can only be amended upon approval by DHR.
- Stipulation IV.C: This stipulation establishes seven distinct Management Zones at Fort Monroe based on a number of factors including careful consideration of historic and existing architectural character, current and past land uses, construction periods, concentration of contributing resources, and resource types such as the Endicott Batteries and individually eligible properties. The Management Zones establish the parameters for demolition of historic buildings; mass, scale, and appropriateness of new construction; and the recommended treatment approach. The Design Standards are more specific guidance on how to operate within those parameters.
- Stipulation IV.D: With the Army presence ending at Fort Monroe, the undertakings occurring there by the Commonwealth or a designated third party will no longer fall under the jurisdiction of Section 106, which pertains strictly to federal projects. Therefore, to ensure consideration and protections in the absence of a federal agency, an entirely new state-level mechanism for evaluating projects occurring at Fort Monroe and their potential to affect historic properties was required. This stipulation establishes a review of undertakings initiated by the Commonwealth or other entity at Fort Monroe. Among the requirements found in this section of the PA are the creation and maintenance of a state position to act as the Fort Monroe Historic Preservation Officer (FMHPO) to act as the subject matter expert, guide project proponents to limit impacts to historic properties, and to coordinate consultation with DHR and other stakeholders. Much like Section 106, undertakings occurring at Fort Monroe sponsored by the Commonwealth or another party must be first reviewed by the FMHPO and then by DHR. This two-tiered review process is intended provide checks and balances to ensure appropriate treatment of significant cultural resources.

Implementation Scenarios
1. Short-term operating lease – The PA will be incorporated into the lease by reference in the lease agreement.
2. Long-term leaseholds – The PA will be incorporated into the leasehold by reference in the leasehold agreement.
3. Long-term leaseholds with prepayment – The PA will be incorporated into the leasehold by reference in the leasehold agreement.
4. Fee simple sales – The PA requires that the property be placed under easement, preservation covenant or other legal enforceable mechanism prior to leaving state ownership or control.

- Historic Preservation Manual and Design Standards – The Fort Monroe Authority (as successor in interest by law to the Fort Monroe Federal Area Development Authority) has developed a Historic Preservation Manual and Design Standards (Design Standards) pursuant to Stipulation III.A of the Programmatic Agreement. These Design Standards are consistent with the PA zone management requirements and its broad treatment directions. They are based upon and consistent with sound and accepted preservation practices and standards established and regularly reviewed in relevant National Park Service publications and guidance documents such as the Preservation Briefs and the Secretary of the Interior’s Standards for the Treatment of Historic Properties with Guidelines for the Treatment of Cultural Landscapes. At a minimum the Design Standards will address all treatment options for historic properties (rehabilitation, restoration, reconstruction and preservation), routine maintenance and repair, appropriate design, massing, height, scale, materials, location, spatial relations, density, etc. for new construction and additions to existing buildings or structures within each Management Zone, significant historic viewsheds and cultural landscapes and the potential to affect archaeological sites resulting from proposed ground disturbing activities. The Design Standards will be reviewed and approved by both the National Park Service and the Virginia Department of Historic Resources. The Design Standards will be the guiding governing document for all architectural review for historic properties and new construction within the National Historic Landmark District regardless of ownership and including properties within the proposed National Park Service Unit boundary. Further, these Design Standards will be applicable to projects proposed on the interior of all historic structures where the contributing historic interior remains intact. They are consistent with the Secretary of the Interior’s Standards for Rehabilitation of Historic Properties which must be followed in order to qualify for both the Federal and State Rehabilitation Tax Credit program.

Implementation Scenarios
1. Short-term operating lease – The Design Standards will be incorporated into the lease by reference in the lease agreement.
2. Long-term leaseholds – The Design Standards will be incorporated into the leasehold by reference in the leasehold agreement.
3. Long-term leaseholds with prepayment – The Design Standards will be incorporated into the leasehold by reference in the leasehold agreement.
4. Fee simple sales – The Design Standards will be recorded in the deed conveyance.

- Community Management Regulations – This is a strategy that was recommended by the Historic Preservation Advisory Group as necessary to complement existing mechanisms to address those community issues normally covered by municipal zoning. FMA’s adoption of community management regulations will take the place of zoning and/or city ordinances and a resident’s manual. Some examples of the types of regulations that will be addressed in the regulation document currently under development by FMA with the assistance of the OAG are landscaping (lawn maintenance, shrub/planting beds, foundation planting, tree replacements, etc.), mailboxes, clotheslines, flags/flagpoles, signs, decorative ornaments, exterior lighting, fences, play equipment (swings, sliding boards, trampolines, basketball goals, etc.), accessory buildings, porches/decks and trash disposals. The regulation document will also address specific requirements for exterior changes not covered by the PA or Design Standards such as trim/details and windows/doors. The regulation will also contain recourse provisions in the event of singular or repeated violations of the regulations.

Implementation Scenarios
1. Short-term operating lease – The regulations will be incorporated as an exhibit to the lease agreement.
2. Long-term leaseholds – The regulations will be incorporated as an exhibit to the leasehold agreement.
3. Long-term leaseholds with prepayment – The regulations will be incorporated as an exhibit to the leasehold agreement.
4. Fee simple sales – The regulations will be a separate document signed at closing of the fee simple deed conveyance. (Subject to confirmation by OAG)

- Historic Easements – Historic preservation easements, a specialized form of conservation easements, are considered the most effective mechanism available for the perpetual preservation of historic resources. An easement is a legally binding and perpetual agreement between a property owner and the easement holding agency. Historic preservation easements are effective because they require that the property be maintained according to a documented condition or better; require that the property owner obtain the prior written approval of the easement holder before undertaking changes; and enable the easement holder to enforce compliance with the terms of the easement. Together, these restrictions promote and enforce appropriate stewardship of the historic property. The deed of easement is recorded at the jurisdictional courthouse and runs with the title to the property. An easement cannot be extinguished except through judicial proceeding, and only then because the easement no longer serves a public purpose, as the resource protected no longer exists.¹ Easements may be amended only in certain circumstances to enhance the

¹ In the 45-year history of DHR’s easement program, only one easement has been extinguished due to casualty loss of the historic building due to fire. In this case, the building was located on a small property that was not within the boundaries of a historic district listed in the Virginia Landmarks Register. In another case, DHR transferred its review authority to the Virginia Outdoors Foundation, who co-held the easement, due to the destruction of the historic house by fire. In this case, DHR retains its right to review ground disturbance for potential impact to

protection of the historic (and perhaps other) resources present.

Easements and Interaction with Other Restrictions

Easements differ from covenants and other restrictive agreements, such as CC&Rs established by a homeowners' association, or even a local historic preservation ordinance. Unlike a covenant, which can be placed on a property for a designated time period, an easement is perpetual in duration. An easement is established to protect defined, significant conservation values (e.g. historic resources) present at a property, and serves a public purpose in doing so. It is carefully crafted to provide appropriate and comprehensive protection for such resources. For example, a historic preservation easement protects the interior and exterior of a historically significant building by requiring that the property be maintained according to a documented standard, and that any changes be consistent with the historic character of the property. Failure on the part of the property owner to comply with such terms would result in a violation of the easement, and an associated enforcement action by the easement holder.

However, unlike a CC&R, an easement does not generally address purely aesthetic issues (such as the color of painted surfaces or acceptable exterior furniture), nor does it address issues, such as noise, that are most often considered under local zoning or a neighborhood agreement. Instead, an easement focuses on preserving the historic integrity of a particular property. Easements and restrictions such as CC&Rs, as well as other control mechanisms, are not mutually exclusive, therefore, and together may provide both satisfactory stewardship of a property and reinforce overall neighborhood objectives.

Importantly, an easement cannot be removed or changed by the vote of a governing board or citizenry, nor can it be influenced by prevailing political or cultural forces. Easements are administered by the professional staff of a governmental agency or private organization whose mission it is to protect and steward the resources. Proposed alterations to an easement property are evaluated by the professional staff according to national standards, such as the Secretary of the Interior's Standards for the Treatment of Historic Properties (Secretary's Standards), to provide a consistent interpretation and application across easement properties. Because of their serious nature, historic preservation and conservation easements, and the agencies that administer easement programs, are highly regulated at the state and federal levels.

Legal Framework

Virginia pioneered the use of easements as a statewide preservation tool. Established by the General Assembly in 1966, Virginia's program today is one of the largest in the country and is viewed as a model nationwide. The General Assembly recognized that the most cost-effective and best preservation of Virginia's historic resources is accomplished when property remains in private ownership, with the Commonwealth ensuring the appropriate protection and stewardship of the property in perpetuity.

The Board of Historic Resources holds easements according to Chapter 22, Title 10.1 and Chapter 17, Title 10.1 of the Code of Virginia which recognize that the preservation of open-

archaeological resources.

space land, including land preserved for historic or scenic purposes, serves a public purpose by curbing urban sprawl and encouraging more desirable and economical development of Virginia's resources. The Department of Historic Resources (DHR) administers the easement program on behalf of the Board of Historic Resources.

Central to the drafting of easement restrictions and administration of easement programs, is the body of Treasury regulations (26 CFR 1.170A-14) which addresses conservation easements. These regulations establish standards for what qualifies as a "perpetual conservation restriction" and "eligible donee," or easement-holding organization. The donee is required to have a commitment to protect the property and the capacity to enforce the terms of the easement. The regulations also set requirements for what constitutes adequate protection of historic properties, including review of proposed changes to ensure compliance with appropriate standards, visual public access, and enforcement of the terms of the easement by the holder.

It is important to note that DHR abides by the requirements set out in Treasury regulations in the management of its program, regardless of whether tax benefits are sought for the donation. In consultation with the Office of the Attorney General and national experts, DHR also engages in regular and thorough review of program policies and procedures and easement template documents, to ensure compliance with all governing state and national laws, and conservation best management practices.

Program Management and Operation

This legal background shapes all aspects of DHR's easement program, from the easement document to management of the program. Each deed of easement is developed from a template document and is tailored to the specific conditions and character of a property. Easement restrictions are crafted to allow a building and property to remain viable, while maintaining and preserving its historic character and the integrity of materials. Following recordation of the easement, all proposed changes are reviewed in a timely manner by DHR's professional staff according to the terms of the easement and in consultation with the Secretary's Standards and associated guidance. DHR's staff, which includes architectural historians, architects, conservationists, and archaeologists, provides guidance to property owners on the appropriate treatment of their historic resources, whether a historic building or structure, cultural landscape, or archaeology.

DHR conducts regular inspections of its easement properties to ensure compliance with the terms of the easement. These monitoring visits also provide an important opportunity to foster a positive relationship with the property owner and to provide technical assistance. Consistent with state and federal law, DHR's easements also require public access and include strong provisions for enforcement of the easement agreement, backed up by the legal authority and resources of the Commonwealth of Virginia, through the Office of the Attorney General.

Violations

If a violation is found to exist at an easement property, DHR assesses the scope and impact of the violation upon the historic character and integrity of the property, and determines the appropriate

enforcement action in close consultation with the Office of the Attorney General (OAG). As outlined in Easement Program Policy #7, “Violations,” DHR establishes a specified time frame for correction of the issue. If the violation is not adequately addressed within the specified timeframe, DHR, through the Office of the Attorney General, will seek all available legal remedies to correct the situation.

DHR works carefully with property owners to ensure the proper stewardship of their historic resources; consequently major easement violations have been rare during the history of the program. When such violations have occurred, DHR strives to achieve a positive resolution that preserves or restores the historic character and integrity of the property. If such resolution cannot be achieved through a constructive relationship with the property owner, DHR seeks appropriate legal action to require that the violation be corrected in an acceptable manner. DHR has successfully brought legal action to require removal of unapproved and inappropriate work, and restoration of a property to its historic appearance.

Easements at Fort Monroe

Simply put, easements are the best tool available to ensure the perpetual preservation of historic resources. While they may not be employed at every building (or historic landscape) at Fort Monroe, an easement held by DHR would guarantee the preservation of the resources thus protected. Easements will be placed on those historic properties that are transferred from state ownership in fee simple, including when a building is transferred in fee-simple with the Commonwealth retaining ownership of the underlying land. So too, for properties transferred out of state control through a long-term leasehold arrangement, a restrictive covenant will be placed on the property for the duration of the lease term, and would resemble an easement in the type of restrictions placed on the property and enforcement capacity.

Easements are an important and effective tool that can be employed for the benefit of the public and historic buildings at Fort Monroe. Importantly, easements can be utilized in conjunction with other restrictions to protect the important historic character of the property and uphold neighborhood objectives.

Implementation Scenarios
1. Short-term operating lease – Not applicable.
2. Long-term leaseholds – A restrictive covenant would be required if any state property (i.e. building improvements) is conveyed out of state control.
3. Long-term leaseholds with prepayment – A restrictive covenant would be required if any state property (i.e. building improvements) is conveyed out of state control.
4. Fee simple sales – A deed of perpetual easement would be recorded to protect property transferred out of state control.

Economic Considerations

The following list identifies a list of economic factors that must be considered in evaluating how the four

scenarios impact the revenue and expenses of the FMA, in particular the funding of capital improvement projects required or needed to upgrade the buildings, infrastructure and utility systems. As mentioned above, the need to provide economic sustainability is critical to the protection of the historic assets. Without an adequate source of operating capital the FMA will not be able to provide for adequate maintenance of the historic assets.

- **Revenue Impact** – The FMA will have ongoing needs to operate and maintain the property. The FMA will also need to raise capital to address the approximately \$35 million in utility and infrastructure upgrades identified during the condition assessment study performed by the civil engineering consultant. The current economic model reflects that the commercial properties will be leased to tenants on operating leases. The residential properties (other than the Wherry apartments) are expected to be leased on operating leases for the first 2-3 years and then converted to long-term prepaid leaseholds over a 6-year period.

Implementation Scenarios
1. Short-term operating lease – Residential operating leases usually have a fixed amount of rental income per month with an annual increase in rent tied to either a fixed percentage or based on some type of consumer price index.
2. Long-term leaseholds – Long-term leasehold agreements usually have a fixed amount of rental income paid quarterly or annually with a periodic increase in rent tied to either a fixed percentage or based on some type of consumer price index.
3. Long-term leaseholds with prepayment – The aggregate amount of rent under the leasehold term would be discounted for the time value of money to determine a net present value (NPV) of the lease. The leaseholder would obtain mortgage financing for the NPV. The FMA would receive the NPV less any marketing/closing costs at the closing of the mortgage. This would result in a one-time revenue contribution from the leasehold with the possible exception of a small transfer fee if the leasehold is transferred to a new owner.
4. Fee simple sales – The FMA and buyer would agree to a sales price for the housing unit. The buyer would either pay cash or obtain mortgage financing for the purchase price. The FMA would receive the proceeds of the sale less any marketing/closing costs. This would result in a one-time revenue contribution from the sale with the possible exception of a small transfer fee if the leasehold is transferred to a new owner.

- **Financing** – The pre-payment of the leasehold rent and the closing of a non-cash sale will require the lessee or buyer to obtain financing for the transaction. The flood plain status may also impact the availability of the lessee/buyer to obtain property insurance through traditional underwriters. Specialty insurance companies do provide property insurance for properties within 100-year flood plains but at a higher premium.

Implementation Scenarios
1. Short-term operating leases – Not applicable.
2. Long-term leaseholds – Not applicable.

<p>3. Long-term leaseholds with prepayment – Based on the BAE report on prepaid leasehold financing the availability of financing for prepaid leasehold transactions may be limited and/or require a significant amount of time and resources from the FMA staff and OAG attorneys to establish a leasehold document that meets the requirement for secondary market lenders.</p>
<p>4. Fee simple sales – Residential mortgage products should be available for buyers of housing units at Fort Monroe based on their individual credit.</p>

- Impact on Capital Improvement Plan funding – The current economic model reflects \$37.3 million of one-time revenue from the prepayment of long-term leaseholds. Of this amount \$25.5 million is projected to go towards site-wide infrastructure and utility upgrades reflected the capital improvement program. The balance of the proceeds are expected to fund operating deficits during the redevelopment of the property including tenant improvements necessary to reposition the commercial space for reuse by new tenants.

Implementation Scenarios
<p>1. Short-term operating leases – Utilizing operating leases on the residential units may help to defray some of the operating deficits but it will not provide a capital source to upgrade the existing infrastructure. Bond underwriters will not generally recognize short-term operating lease revenue as adequate security for a revenue bond issuance.</p>
<p>2. Long-term leaseholds – Long-term leasehold revenue will provide a stable revenue stream for the term of the lease. This revenue stream may be sufficient to underwrite a revenue bond issuance to provide funding for capital improvement projects. Bond proceeds would be eligible to be used for capital improvement projects but may not be used for operating expenses.</p>
<p>3. Long-term leaseholds with prepayment – This is the strategy currently reflected in the economic model. It is anticipated, based on current market conditions and estimates of property values, that the prepaid leasehold program would generate approximately \$37 million. This revenue would be unrestricted and could fund either capital improvement projects or operating expenses.</p>
<p>4. Fee simple sales – If fee simple sales were authorized, the FMA would realize higher revenues than currently reflected in economic model. The current economic model discounts leasehold sales by 10 percent, so the FMA would potentially realize \$3.7 million in higher revenues under a fee simple program and could realize these revenues sooner than under a leasehold program since it would avoid having to establish sources of financing for leasehold sales. Revenue from fee simple sales would be unrestricted and could be used for capital improvement projects or operating expenses.</p>

- Maintenance and Repair – The 174 family housing units at Fort Monroe are largely in good condition. However, the cost to maintain historic homes to the Secretary of the Interior Standards for the Treatment of Historic Properties is higher than the maintenance costs for new housing

units. Based on statistics collected from industry sources such as the Building Owners and Management Association (BOMA), it is estimated to cost approximately \$3,000 annually per unit for maintenance and repair. This represents approximately \$522,000 in annual costs to the FMA if all the units are leased on short-term operating leases. In any scenario, all maintenance and repair activities for historic properties will be subject to the provisions of the Secretary’s Standards and other governing documents.

Implementation Scenarios
1. Short-term operating leases – The cost for maintenance and repair would be the responsibility of the FMA. These costs would be an operating expense that offset the rental revenue for the housing units.
2. Long-term leaseholds – The cost of maintenance and repair would be transferred to the leaseholder under the provisions of the leasehold agreement.
3. Long-term leaseholds with prepayment – The cost of maintenance and repair would be transferred to the leaseholder under the provisions of the leasehold agreement.
4. Fee simple sales – The cost of maintenance and repair would be the responsibility of the property owner.

- Property Insurance – One of the key economic aspects of protecting historic property at Fort Monroe is to ensure that it is adequately insured. All of the property at Fort Monroe lies in the 100-year flood plain. If property remains under the ownership of the Commonwealth then the property would be insured through the Virginia Department of Risk Management (DRM). While the state program is self-insured for losses below \$5 million, the state has created a program for properties at Fort Monroe with a traditional deductible at \$5,000 per occurrence. If building improvements are transferred to the leaseholder or buyer as part of the leasehold or sales agreement then the burden of obtaining property insurance would fall on the leaseholder. While the BAE feasibility report indicated that property insurance may be hard to obtain from traditional homeowner insurance companies, there are specialty insurance companies who will issue insurance on property within the 100-year flood plain, although at higher premiums.

Implementation Strategies
1. Short-term operating leases – The cost for property insurance would be the responsibility of the FMA. These costs would be an operating expense that offset the rental revenue for the housing units.
2. Long-term leaseholds – If the building improvements remain as Commonwealth property then the property would be insured under the Virginia DRM but the cost of the premium would be billed to the leaseholder. If the building improvements are transferred to the leaseholder as part of the leasehold agreement then the burden to obtain property insurance would be the responsibility of the leaseholder under the provisions of the leasehold agreement.
3. Long-term leaseholds with prepayment – If the building improvement remain as Commonwealth property then the property would be insured under the Virginia DRM but the cost of the premium would be billed to the leaseholder. If the building

improvements are transferred to the leaseholder as part of the leasehold agreement then the burden to obtain property insurance would be the responsibility of the leaseholder under the provisions of the leasehold agreement.
4. Fee simple sales – The cost of property insurance would be the responsibility of the property owner.

- Payment in Lieu of Taxes (PILOT) – The 2011 Fort Monroe Authority Act (2011 SB1400) sets out a mechanism for the FMA to make semi-annual payments to the City of Hampton in exchange for the City’s provision of municipal services typically available to private property owners in the City. These services include police, fire, emergency response, public education, parks and recreation, social services, libraries, animal control, voter precincts, court and other services. The PILOT is the equivalent of the real estate tax based on City assessment of property at Fort Monroe at current real estate tax rate for private property owners in the City.

Implementation Scenarios
1. Short-term operating leases – The value of the parcel would be included in the FMA’s assessed value for calculating the PILOT fee to the City of Hampton.
2. Long-term leaseholds – The leaseholder would be responsible for paying real estate taxes to the City based on the assess value of the property at the City’s current millage rate. The assessed value is decreased once the remaining term of the leasehold is less than 50 years, eventually stabilizing at 15% of the assessed value if the term is less than 20 years. [See VA Code § 58.1-3203]
3. Long-term leaseholds with prepayment – The leaseholder would be responsible for paying real estate taxes to the City based on the assess value of the property at the City’s current millage rate. The assessed value is decreased once the remaining term of the leasehold is less than 50 years, eventually stabilizing at 15% of the assessed value if the term is less than 20 years. [See VA Code § 58.1-3203]
4. Fee simple sales – The property owner would pay real estate tax based on the assessment of the property at the City’s current millage rate.

- Marketability – One of the items evaluated by David Shiver in the BAE leasehold feasibility report was the marketability of residential long-term leaseholds in the Hampton Roads market. Based on interviews with residential brokers on the Peninsula and Southside Shiver learned that there are no residential single-family leasehold properties in the market. The brokers also indicated that leaseholds would need to be essentially perpetual to be an attractive alternative for homeowners used to fee simple sales. This may limit the restrictions that could be placed in the leasehold agreement.

Implementation Scenarios
1. Short-term operating leases – The FMA is currently marketing short-term leases for residential properties. For smaller properties, a short-term lease would be attractive; for some of the large homes at Fort Monroe, tenants will likely seek longer-terms

arrangements.
<p>2. Long-term leaseholds – Marketing long-term residential leaseholds with annual payments would present potential marketing challenges. Rent would have to be set to be competitive with homeownership for a property of comparable value (e.g., 4 to 5 percent of the value of land and improvements per year). The long-term leaseholder would not have the same equity build-up potential as would be possible under the prepaid leasehold option, since under this option there likely would be periodic adjustments to rent to reflect changes in property value or CPI. The FMA would have to educate local brokers and potential leaseholders about this leasehold product. The depth of market for high-end residential rentals in the Hampton Roads market may be limited to support this type of leasehold program. [Note: The FMA’s rate of return would be constrained by then current mortgage market. If the average conforming rate is 4.5%, that will limit the amount the FMA may be able to charge as base rent as a percent of total property value. Otherwise leaseholds at Fort Monroe would be more expensive than buying similar properties elsewhere.]</p>
<p>3. Long-term leaseholds with prepayment – Based upon the findings of the BAE Report, successful marketing long-term leaseholds with prepayment would be contingent upon establishing a financing program that is acceptable to lenders and the secondary market. In addition, the FMA would have to educate local residential brokers and prospective buyers about this leasehold product. Overall, long-term leaseholds with prepayment would have to be structured to resemble as closely as possible a fee-simple sale to reduce the number of marketing objections from prospective buyers. For example, a key attribute cited by residential brokers would be to make the lease “perpetual.”</p>
<p>4. Fee simple sales – A fee simple would be familiar to brokers and prospective buyers and would face the standard types of issues associated with marketing residential real estate (e.g., property conditions, local schools, and level of taxation). The FMA would have to educate local brokers about historic preservation easements and other requirements that would be considered unique in the Hampton Roads region.</p>

The following chart summarizes the applicability of the various protection tools and the impact on each strategy on the economic operation of Fort Monroe.

	Operating Lease	Leasehold	Prepaid Leasehold	Fee Simple Sale
Preservation and Community Strategies				
Programmatic Agreement	Terms of PA would be incorporated by reference in the lease agreement	Terms of PA would be incorporated by reference in the leasehold agreement	Terms of PA would be incorporated by reference in the leasehold agreement	PA requires that property be placed under easement, protective covenant, or other legally enforceable mechanism prior to property leaving state ownership of control
Historic Preservation Manual and Design Standards	Design Standards will be incorporated by reference in the lease agreement	Design Standards will be incorporated by reference in the leasehold agreement	Design Standards will be incorporated by reference in the leasehold agreement	Design Standards will be recorded in the deed conveyance
Community Management Regulations	Regulations will be incorporated by reference in the lease agreement	Regulations will be incorporated by reference in the leasehold agreement	Regulations will be incorporated by reference in the leasehold agreement	Regulation restrictive agreement document would be signed at closing
Historic Easements	Not Applicable	Not Applicable unless improvements are conveyed to leaseholder then a restrictive covenant for the term of lease would be recorded for any property conveyed out of state control	Not Applicable unless improvements are conveyed to leaseholder then a restrictive covenant for the term of lease would be recorded for any property conveyed out of state control	Deed of perpetual easement recorded to protect property transferred out of state ownership

	Operating Lease	Leasehold	Prepaid Leasehold	Fee Simple Sale
Economic Considerations				
Revenue Impact	FMA would receive rental income on a monthly basis. Leases usually include an annual increase.	FMA would receive rental income, typically on a quarterly or annual basis. Leases usually include an annual increase.	FMA would receive a lump-sum payment on closing of mortgage financing. FMA may be able to collect a small transfer fee if leasehold is transferred to new leaseholder.	FMA would receive a lump-sum payment on closing of mortgage financing. FMA may be able to collect a small transfer fee if leasehold is transferred to new leaseholder.
Financing	Not Applicable	Not Applicable	Uncertain. Termination of lease limited to instances of monetary default to meet secondary market lending requirements.	Available based on buyer's credit.
Impact on Capital Improvement Plan	Short-term operating leases would not provide a long-term revenue stream that could be used to underwrite a revenue bond issuance.	Long-term aspect of rental payments may provide adequate security for a revenue bond issuance. Bond proceeds are typically limited to capital projects and may not fund non-capital expenses.	Discount to fee simple value is estimated to be 10%-20% depending on restrictions in leasehold. Payments received would not be restricted as with bond proceeds.	Proceeds from sale of property would be used to fund capital improvement projects. Payments received would not be restricted as with bond proceeds.
Maintenance and Repair (M&R) Costs	Gross leases obligate the FMA to pay M&R, insurance and PILOT.	M&R, insurance and real estate tax expense would be the responsibility of the leaseholder.	M&R, insurance and real estate tax expense would be the responsibility of the leaseholder.	M&R, insurance and real estate tax expense would be the responsibility of the leaseholder.

	Operating Lease	Leasehold	Prepaid Leasehold	Fee Simple Sale
Economic Considerations				
Insurance	Properties would remain state-owned property covered by VA Department of Risk Management insurance program. FMA would be responsible for insurance premiums.	Depending on decision about transferring improvements, properties may remain state-owned property covered by VA Department of Risk Management insurance program. Leaseholder would be responsible for insurance premiums.	Depending on decision about transferring improvements, properties may remain state-owned property covered by VA Department of Risk Management insurance program. Leaseholder would be responsible for insurance premiums.	Property insurance would be the responsibility of the property owner.
Payment in Lieu of Taxes (PILOT)	Assessed value of property would be included in the calculation of the PILOT fee payable to the City of Hampton.	Leaseholder would be responsible for paying real estate tax directly to City of Hampton. VA Code limits taxation of leaseholds with remaining terms below 50 years.	Leaseholder would be responsible for paying real estate tax directly to City of Hampton. VA Code limits taxation of leaseholds with remaining terms below 50 years.	Owner would be responsible for paying real estate tax directly to City of Hampton.
Marketability	Short-term operating leases would likely be accepted by tenants for the smaller homes. Tenants interested in the larger homes would likely request longer-term operating leases.	Brokerage community focus groups indicated leasehold must be effectively perpetual.	Brokerage community focus groups indicated leasehold must be effectively perpetual.	Fee simple sales are understood and accepted in the local market.

Conclusions

No conclusions were drawn by the sub-group at its meeting on May 24, 2011. The LFWG met to review the report on June 21, 2011. No conclusions were made at that meeting. The LFWG will meet again on July 14, 2011. The Chair of the LFWG asked the representatives of the Citizens for a Fort Monroe National Park to present a report on their proposed strategy at the next LFWG meeting.

Recommendations

The Chairman of the FMA Board of Trustees has requested that the LFWG make a recommendation on strategy to the FMA Board at its meeting in November 2011.