

**Lighthouse Realty Services, Inc.**

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December 3, 2011

City of Key West  
Mr. Mark Finigan  
Assistant City Manager  
525 Angela Street  
Key West, FL 33040

Re: Caribbean Spa Building, a 22 room hotel and spa located at 529 Front Street, Key West, Florida 33040.

Dear Mr. Finigan:

I have prepared a letter at your request in response to an offer that was made on September 2, 2011 of the above referenced property. This assignment is considered a consulting assignment and the purpose of this letter was to determine if the offer price was reasonable. The effective date of this consulting assignment is November 30, 2011.

The property is located at 529 Front Street within the City of Key West, Monroe County, Florida. It consists of a two-story, 22 room hotel known as the Caribbean Spa Building. It is currently leased to the Pier House Resort and Caribbean Spa and is being operated in conjunction with the entire hotel and resort. The Pier House Resort is an upper end full service hotel that contains a total of 142 rooms including the subject rooms located at One Duval Street. The subject building was completed/renovated in 1989 and was in good condition. The property was upgraded and the FF & E (Furniture, Fixture & Equipment) was replaced in 2008. The land parcel contains 0.497 acres or 21,640 square feet and is zoned HRCC-1, Duval Street Gulfside District, by the City of Key West, Florida. The subject is under a long term ground lease from the City of Key West to the Pier House Joint Venture. The lease was assumed in August 1987 and expires on May 31, 2020. The annual lease payment is only \$3,600 per year, which is well below market rates.

I was engaged earlier in the year by the current client to appraise the property for possible sale purposes. The effective date of that appraisal was as of April 25, 2011. Since that appraisal the client received an offer dated September 2, 2011 from the lessee to purchase the property.

The prior appraisal estimated: the Market Value of the subject property as a stand-alone property based on the total assets of the business (i.e. tangible and intangible assets) or going concern as a hotel as a Fee Simple Estate, the Market Value of the subject property as a Leased Fee Estate, and the Market Value of the Leasehold Interest.

As discussed earlier, the property is under a long term ground lease to the Pier House and the lease will expire on May 31, 2020. This lease is below market and there is a leasehold position. The appraiser requested operational data from the Pier House Resort & Caribbean Spa in order to value the property under several scenarios for the fee simple client, which is the City of Key West. In the appraisal performed as of April 25, 2011, the hotel operator provided the appraiser with only the three year averages of the Caribbean Spa Building (subject property) ADR, (Average Daily Rate), Occupancy and RevPAR. The appraiser requested operating data for the entire hotel operation as well as separate allocations for revenue and expenses from the spa and meetings rooms. This information was not provided to the appraiser.

The appraiser was requested to also value the property based as a going concern as a hotel with the benefit of the Pier House Resort and Caribbean Spa as a whole in the fee simple estate. However, this approach was not utilized since I was unable to obtain the information. In the prior appraisal, under a hypothetical assumption, I valued the property in fee simple assuming the subject was a stand-alone property of 22 units (transient) and is not affiliated with the Pier House. The property was appraised under a hypothetical assumption in which I had allocated capital needed for startup cost as a stand-alone hotel. Further, the meeting rooms would be leased to a third party for use as a restaurant or retail use, as meeting rooms would not be needed for a small hotel.

For the fee value, the appraiser's projections of revenue and expenses, was based on a combination of the income of the subject provided as a whole, along with current market data from nearby competitive hotels. The appraiser was able to extract market data from discussions with local hotel managers, Star Reports, and office files.

To recap, the appraisal concluded that there was significant leasehold value in the property due to the below market lease. The concluded values relevant to this consulting assignment are the Fee Simple and Leased Fee values. The conclusion of the subject as a stand-alone property based on the total assets of the business or a going concern as a hotel under the Fee Simple Estate was \$7,000,000. The Market Value of the subject property as encumbered by the existing lease (Leased Fee Estate) was \$4,700,000.

I was provided a letter of intent from the City of Key West to consider for this assignment. The lessee, Pier House Joint Venture submitted a letter of intent dated September 2, 2011 for the purchase of the property for \$6,300,000. The offer had no conditions or contingencies with this bid.

The offer price is well above the Leased Fee value and below the concluded hypothetical fee value. In the prior appraisal the FF& E (Furniture Fixtures & Equipment) was allocated \$425,000, which would reduce the property fee value for the real estate only at \$6,575,000. Since the property is under a current lease, the Leased Fee value would be more appropriate for most investors. The current lease impacts the fee simple value significantly due to the fact the lease payments are well below market. The leaseholder has a vested interest in the property and is offering to pay a premium due to the additional benefits to their adjacent resort operation.

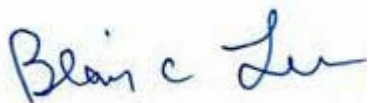
This report has been prepared for the City of Key West. The intended use was to assist the client in determining if a recent offer from the lessee is considered reasonable. The scope of work performed is specific to the needs of the intended user and the intended use. No other use is intended, and the scope of work may not be appropriate for other uses.

As a result of my investigation and analysis of the information obtained therefrom the client as well as the prior appraisal, the offer made to the City of Key West appears to be reasonable based on the fact they are paying well above the appraised Leased Fee Value since there is a significant below market lease in place. I would also recommend that the City of Key West make a higher counter offer as the lessee has a desire to prohibit any others from purchasing the property.

Your attention is directed to the Limiting Conditions and underlying assumptions upon which the analysis and conclusions are contingent. It is my opinion that the following consulting report has been prepared in conformity with the Uniform Standards of the appraisal practice (UAPAP).

Should you have any questions regarding this report, please do not hesitate to contact me.

Respectfully submitted,

A handwritten signature in blue ink that reads "Blair C. Lee". The signature is written in a cursive, flowing style.

Blair C. Lee, MAI  
State Certified General Real  
Estate Appraiser, No. RZ2125

BCL (File 11-201)

### **Purpose of Assignment**

The purpose of the letter is to determine if the recent offer made by the lessee was reasonable.

### **Intended Use**

The client, City of Key West is considering a recent offer for possible sale purposes on the property and has requested an opinion from the appraiser based on the fact it was appraised in April 2011.

### **Market Value**

According to the agencies that regulate federal financial institutions in the United States of America (FIRREA), *Market Value* is defined as "the most probable selling price in terms of money which a property should bring in a competitive and open market under all conditions requisite to be fair sale, the buyer and seller, each acting prudently, knowledgeably, and assuming the price is not affected by undue stimulus".

Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

1. Buyer and seller are typically motivated;
2. Both parties are well informed or well advised, and each acting in what he considers his own best interest;
3. A reasonable time is allowed for exposure in the open market;
4. Payment is made in cash in U.S. dollars or in terms of financial arrangements comparable thereto; and
5. The price represents a normal consideration for the property sold unaffected by special financing or creative financing or sales concessions granted by anyone associated with the sale.

### **Property Rights Definitions**

Fee Simple Estate, Leased Fee Estate and Leasehold Interest are defined as follows: (The Dictionary of Real Estate Appraisal, 5th Edition, Appraisal Institute 2010):

**Fee Simple Estate:** Absolute ownership subject only to limitations imposed by the State; also called a freehold.

**Leased Fee Estate:** A freehold (ownership interest) where the possessory interest has been granted to another party by creation of a contractual landlord-tenant relationship (i.e., a lease).

**Leasehold Interest:** The tenant's possessory interest created by a lease.

The subject parcel is encumbered by a long term ground lease that began in 1965. The current tenant (lessee) assumed the lease in August 1987. The current lease is under the ownership of the Pier House Lease Joint Venture. The lease calls for annual payments of \$3,600 per year and the tenant is responsible for all expenses and upkeep. The lease expires on May 31, 2020. Due to the low rent payment there is a leasehold position of the tenant or lessee.

### Extraordinary Assumptions

Extraordinary assumptions are defined by the Uniform Standards of Professional Appraisal Practice as "...an assumption, directly related to a specific assignment, which, if found to be false, could alter the appraiser's opinions or conclusions. Extraordinary assumptions presume as fact otherwise uncertain information about physical, legal or economic characteristics of the subject property; or about conditions external to the property, such as market conditions or trends; or about the integrity of data used in an analysis." This appraisal employs the following extraordinary assumptions:

None.

### Hypothetical conditions

Hypothetical conditions are defined by the Uniform Standards of Professional Appraisal Practice as "...that which is contrary to what exists but is supposed for the purpose of analysis. Hypothetical conditions assume conditions contrary to known facts about physical, legal, or economic characteristics of the subject property; or about conditions external to the property, such as market conditions or trends; or about the integrity of data used in the analysis." This appraisal employs the following hypothetical conditions:

The property is currently under a long term ground lease to the Pier House and the lease will expire on May 31, 2020. This lease is below market and there is a leasehold position. In the prior appraisal, the appraiser requested operational data from the Pier House Resort & Caribbean Spa in order to value the property under several scenarios for the fee simple client, which is the City of Key West. This information was not provided. I had appraised the property in fee simple assuming the subject is a stand-alone property of 22 transient units and is not affiliated with the Pier House. The property was valued by estimating startup cost and leased the meeting rooms to a third party for a restaurant or commercial type use.

### **Legal Description**

The legal was obtained by a survey prepared by Frederick H. Hilderbrandt, Job No 06-335; last updated June 14, 2006. The subject legal is that part of Lot 1, Square 2 according to William A. Whitehead's map of the Island of Key West, delineated in February 1829 in the Public Records of Monroe County, Florida and is described as follows:

Beginning at the intersection of the westerly line of Simonton Street and the northerly line of front street; thence run westerly along the northerly line of Front Street, 88 feet 4 inches to Lot 2 of said Square; thence run at right angles Northerly and parallel with Simonton Street a distance of 245 feet; thence run at right angles and parallel with front street a distance of 88 feet, 4 inches back to said westerly line of Simonton Street; thence run along the said westerly line of Simonton Street, a distance of 245 feet to the point of beginning, containing .0497 acres, more or less.

### **Preface to Value/Scope of the Assignment**

In preparing this letter, I have relied upon the offer provided by the client, and used information that was contained in an appraisal that I performed on this property in April 2011. I have complied with Standards Rule 4 in regards to consulting assignments. The information in regards to the offer was presented earlier in the body of the letter.

## CERTIFICATION

I certify that, to the best of my knowledge and belief:

- \* the statements of fact contained in this report are true and correct.
- \* the reported analysis, opinions, and conclusions are limited only by the reported assumptions and limiting conditions, and are my personal, impartial, and unbiased professional analyses, conclusions and recommendations.
- \* I have no present or prospective interest in the property that is the subject of this report, and I have no personal interest with respect to the parties involved.
- \* I have no bias with respect to any property that is the subject of this report or to the parties involved in this assignment.
- \* My engagement in this assignment was not contingent upon developing or reporting predetermined results.
- \* My compensation for completing this consulting assignment is not contingent upon the developing or reporting of a predetermined value or direction in value that favors the cause of the client, the amount of the value opinion, the attainment of a stipulated result, or the occurrence of a subsequent event directly related to the intended use of this assignment or appraisal.
- \* My analyses, opinions and conclusions were developed, and this report has been prepared, in conformity with the Uniform Standards of Professional Practice adopted by the Appraisal Standards Board of Appraisal Foundation.
- \* No one provided significant professional assistance to the person signing this report.
- \* I currently hold an appropriate state license or certification allowing the performance of real estate appraisals in connection with federally related transactions.
- \* I appraised this property for the current client with an effective date as of April 25, 2011.

As of the date of this appraisal I have completed the continuing education program of the Appraisal Institute.

Respectfully submitted,



Blair C. Lee, MAI  
State Certified General Real  
Estate Appraiser, No. RZ2125

## **ASSUMPTIONS AND LIMITING CONDITIONS**

The value conclusion and certification within this report are made expressly subject to the following assumptions and limiting conditions as well as any further reservations or conditions stated within the text of the report.

- 1) No responsibility is assumed for the legal description or for matters including legal or title considerations. Title to the property is assumed to be good and marketable.
- 2) All existing liens and encumbrances, (except the existing leases if any) have been disregarded, and the property is appraised as though free and clear.
- 3) Responsible ownership and competent property management are assumed.
- 4) The information furnished by others is believed to be reliable. However, no warranty is given for its accuracy.
- 5) All engineering is assumed to be correct. The plot plans and illustrative material in this report are included only to assist the reader in visualizing the property.
- 6) It is assumed that there are no hidden or unapparent conditions of the property, subsoil, or structures that render it more or less valuable. No responsibility is assumed for such conditions or for arranging for engineering studies that may be required to discover them.
- 7) It is assumed that there is full compliance with all applicable federal, state, and local environmental regulations and laws unless non-compliance, is stated, defined, and considered in the appraisal report.
- 8) It is assumed that all applicable zoning and use regulations and restrictions have been complied with, except where non-conformity has been stated, defined, and considered in the appraisal report.
- 9) It is assumed that all required licenses, certificates of occupancy, consents, or other legislative or administrative authority from any local, state, or national government or private entity or organization have been or can be obtained or renewed for any use on which the value estimate contained in this report is based.



**ASSUMPTIONS AND LIMITING CONDITIONS** (Continued)

- 10) It is assumed that the utilization of the land and improvements is within the boundaries of property lines or the property described and that there is no encroachment or trespass unless noted in this report.
- 11) Subsurface rights were not considered in making this appraisal.
- 12) The distribution, if any, of the total valuation of this report between land and improvements applies only under the stated program of utilization. The separate allocations for land and buildings must not be used in conjunction with any other appraisal and are invalid if so used.
- 13) Possession of this report, or a copy thereof, does not carry with it the right of publication. It may not be used for any purpose by any person other than the party to whom it is addressed without the written consent of the appraiser, and in any event only with proper written qualification and only in its entirety.
- 14) The appraiser herein by reason of this appraisal is not required to give further consultation, testimony, or be in attendance in court with reference to the property in question unless arrangements have been previously made.
- 15) Neither all nor any part of the contents of this report (especially any conclusions as to value, the identity of the appraiser, or any reference to the MAI or SREA designations) shall be disseminated to the public through advertising, public relations, news, sales, or other media without the prior written consent and approval of the appraiser.
- 16) The existence of any environmental hazard such as the presence of hazardous wastes, toxic substances, radon gas, asbestos containing materials, ureaformaldehyde insulation, etc., which may or may not be present in or on the subject property or any site within the vicinity of the property was not observed and knowledge of any such environmental hazard is not assumed. The appraiser is not qualified to detect such substances. The concluded market value is predicated on the assumption that there is no such material on the property that would cause a loss in value.

**ASSUMPTIONS AND LIMITING CONDITIONS** (Continued)

- 17) Unless specifically stated to the contrary in the report, no independent evaluation of concurrency matters were made for the subject or any sales comparables. In the event concurrency is found to affect subject property or any of the sales comparables, we reserve the right to reconsider the value conclusion.
- 18) This appraisal was not based on a requested minimum valuation, a specific valuation, or the approval of a loan.
- 19) The Americans with Disabilities Act (ADA) became effective January 26, 1992. The appraiser has not made a specific compliance survey and analysis of this property to determine whether or not it is in conformity with the various detailed requirements of the ADA. It is possible that a compliance survey of the property together with a detailed analysis of the requirements of the ADA could reveal that the property is not in compliance with one or more of the requirements of the act. If so, this fact could have a negative effect upon the value of the property. Since the appraiser has no direct evidence relating to this issue, he did not consider possible noncompliance with the requirements of the ADA in estimating the value of the property.