Forum: For Minnesotans, the overtime waters just got treacherous • D3

BUSINESS INSIDER

www.startribune.com/business

Star Tribune

Monday, August 16, 2004 • Section D

Managing: Hidden riches
Making lemonade out of lemons – in the form of dirty scrap metal. **D4**

Small Biz: No niche for me
How to avoid getting typecast as a business. **D5**

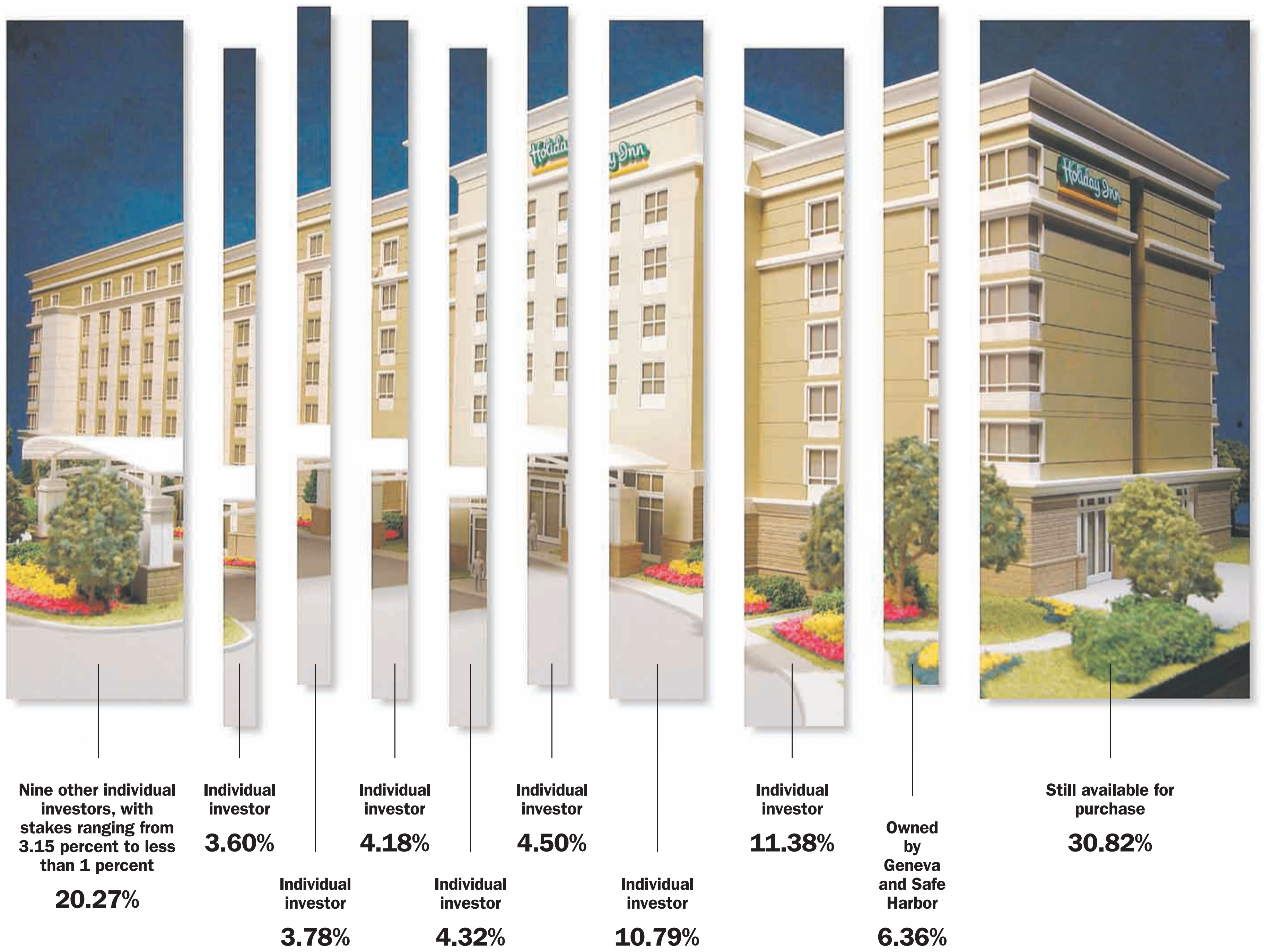
Selling it: Unified whole
A new degree program offers the complete PR package. **D7**

Edge: Stays cool in the heat

Flame-resistant plywood could be a welcome sight in West Coast homes. **D8**

Getting in on the ground floor ... or the fifth floor ... or the east wing ...

Through the Safe Harbor Web site, investors can buy finely diced pieces of commercial properties. Here's the ownership breakdown for a $22 million Holiday Inn and water park that is to be built in Otsego, Minn. Safe Harbor/Geneva takes an equity stake; brokerage fees total $463,873. Prices for the individual stakes sold thus far range from $189,844 to $2.5 million.



Buying a little piece of a big deal

By Terry Fiedler
Star Tribune Staff Writer

Michael Houge and Keith Sturm knew they had a good thing going when they arrived in their office on a number of mornings recently and found a few million dollars in letters of intent for the retail properties they offered over the Internet.

In fact, their Minneapolis-based Upland Net Lease Sales has seen gross volume grow from about $10 million in 1998 to a projected $125 million this year, Houge said.

But they also were certain that an even bigger opportunity waited in a similar market.

Rather than just selling properties for a few million dollars each to single buyers, as they do with Upland, Houge and Sturm have partnered with Minneapolis real estate entrepreneur Duane Lund, managing partner of the Geneva Organization, to also sell properties sliced into portions costing as little as $100,000 each.

The new company, called Safe Harbor Properties Exchange, is projecting first-year, 2004 sales volume of about $100 million to $125 million in so-called tenant-in-common (TIC) deals, and at least double that next year.

"The [Upland] business keeps humming," Houge said, "but in the next year-and-a-half the TIC business will overshadow that. The appetite is so much bigger."

Fractionalized sales of commercial properties have exploded in recent years, a trend that is largely tied to baby boomer business owners looking to sell out and reinvest in a tax-deferred investment vehicle called a 1031 property exchange, and to a clarification of tax law in 2002.

The amount of equity invested in fractionalized commercial real estate, or TICs, has grown from $156 million nationally in 2001 to an estimated $2 billion this year, according to Utah-based Omni Brokerage. Including the loaned portion of the deals, the value of TIC deals is expected to reach $5 billion to $6 billion this year.

Houge said the industry is considerably bigger, though, because Omni counts only TIC deals that are sold through securities brokers.

Lund estimated that the entire 1031 property exchange market is about $50 billion a year and that TICs eventually could capture about 20 percent of that.

The number of firms offering the fractionalized TIC deals also has jumped, from nine in 2001 to more than 35 nationally this year, according to industry estimates. Among the pioneers in the TIC industry is St. Paul-based AEI Capital Corp.

Given the influx of new firms, AEI Executive Vice President Rick Vitale cautioned that some will honor their fiduciary responsibilities, but that others will act simply as "property flippers."

FRACTIONS continues on D6:
— Deals are popular for exchanges.

Food firms keep eye on pyramid update

Getting their share at the market

Here's what's at stake for food companies as the Food and Drug Administration considers overhauling its food pyramid:

If the pyramid recommends less carbohydrates and more protein in a diet, grain-based foods such as breads, pasta and rice will lose out while chicken, beef and eggs will gain prominence.

If the pyramid focuses on removing salt and sugar from a diet, snack foods such as potato chips, pretzels, peanuts and sweetened beverages will lose out.

If the pyramid emphasizes the benefits of omega-3 fatty acids, then fish will be a winner.

The USDA is finalizing revisions to the food pyramid, scheduled to be introduced in '05.

By Thomas Lee
Star Tribune Staff Writer

The food pyramid, that ubiquitous symbol of American nutrition for the past 12 years, is being tweaked. And food companies, from General Mills Inc. to Kraft Inc., are watching carefully.

The U.S. Department of Agriculture (USDA) is in the final stages of revising the pyramid, first introduced in 1992 as a rough visual guide to what and how much Americans should eat each day. The new version is scheduled to be introduced in mid-2005, and food manufacturers are on high alert for any changes that could be detrimental to their products.

"As an issue, there's few that's bigger," said Gene Grabowski, a former vice president of the Grocery Manufacturers of America, one of the industry's largest lobbying groups. In an industry that lives and dies by labels, "it doesn't take much to suggest that a food type isn't the best food to be eaten," said Grabowski, now an executive with Levitt Strategic Communications, a Washington, D.C., consulting firm that works closely with food companies.

PYRAMID continues on D7:
— Grain-based companies such as General Mills might have the most to lose.
— Atkins proponents would like to see less weight given to grain-based foods.
— Long overdue for overhaul.

INSIDE TRACK

The doctor is in

The Twin Cities commercial office market remains in one of its biggest funks in decades, with at least one notable exception — **medical space**.

The second-quarter vacancy rate for on- and off-campus medical office space was 8.3 percent, according **Grubb & Ellis/Northco Real Estate Services.** Contrast that with an overall office vacancy rate in the metro area of around 20 percent.

Jill Rasmussen, senior vice president-healthcare for Grubb & Ellis/Northco, said the medical market normally avoids the big vacancy swings of the office and industrial markets.

Medical office tenants are usually financially healthy and stable, and they tend to commit to spaces for much longer periods than other kinds of tenants. Fifteen-year leases are not uncommon, she said.

Looking ahead, she sees medical office building activity ramping up substantially in the next several months as the big health care organizations try to create more of a retail presence in the faster-growing suburbs with new clinical and surgical facilities.

FUNNY MONEY: Don't be surprised if you get some funny money in your change over the next few weeks. **Boodle**, an online coupon service, is testing some guerrilla-marketing tactics in Minneapolis.

To drive Internet traffic, Boodle is circulating 16,000 marked quarters in change machines, pay phones and vending machines throughout the city. Each quarter bears a removable sticker with a marketing message and a Web address.

Marked money might be catching on as a marketing device. According to **Ad Age** magazine, Boodle's gimmick is the second time the tactic has been used recently. Earlier this year, **USA Networks** put stickers on 50,000 one-dollar bills to promote the miniseries "Traffic."

INSIDE TRACK continues on D7

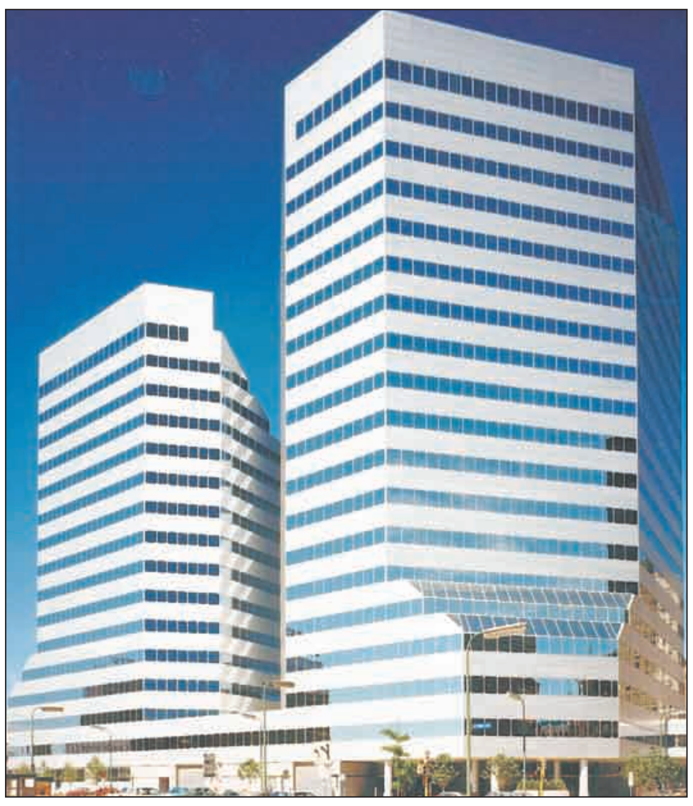
Have some news for **Inside Track?** *Call 612-673-4237 or send us an e-mail at* **insider@startribune.com**

R W B G Y X 1 2 3 4 5 6 7

Copyright 2004 Star Tribune. Republished with permission of Star Tribune, Minneapolis-St. Paul. No further republication or redistribution is permitted without the written consent of Star Tribune

HOT PROPERTY

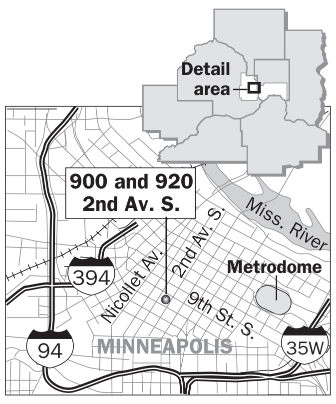
from the Minnesota Real Estate Journal



Welsh Cos.

International Centre I & II

900 and 920 2nd Av. S., Minneapolis



Square feet: 614,193
Floors: 20 and 17
Buyer: Welsh Companies
Seller: Travelers Insurance Co. affiliate
Details: The recent acquisition of International Centre I and II marks Welsh's first foray into office ownership in the Minneapolis central business district.

The Bloomington-based firm plans to aggressively market the towers, which are about 35 percent occupied. Up for grabs is naming rights on both buildings.

The largest contiguous space is about 150,000 square feet, and the floor plates are about 18,000 square feet. Welsh, which will handle leasing and management for the property, also has plans for $1 million in lobby improvements.

Welsh Senior Vice President Mike Perkins said the firm expects to take advantage of a market that appears to have hit bottom. The office vacancy rate is still about 20 percent, but the absorption rate, which has been negative for the past couple of years, appears to be flattening.

"It's not trending down anymore," he said. "There are no new buildings that are going to be built. The trend ultimately will go up, space will fill up and there will be a healthier downtown from the landlord's perspective."

In addition to Perkins, members of the International Centre leasing and management team are Nils Snyder, senior associate; Greg Moltumyr, associate; and Larry Barnett, general manager.

Welsh owns nearly 7 million square feet of office, industrial and retail space in the Midwest.

Danielle Anderson

The Minnesota Real Estate Journal *is published monthly.*
Web site: *http://www.rejournals.com*

NOTABLE TRANSACTIONS

7550 France Av. S.
Edina
$11,600,000
Filing date: 6/9/2004
Seller: Northwestern Mutual Life Insurance.
Buyer: Edina Business Plaza LLC
Property ID: 3102824410240

4625 W. 77th St.
Edina
$8,000,000
Filing date: 6/23/2004
Seller: Northwestern Mutual Life Insurance.
Buyer: Seagate Technology LLC
Property ID: 0602724220014
Property ID: 3102824340002
Property ID: 3102824340003
Property ID: 3102824340004
Property ID: 3102824340005

7705 Egan Dr.
Savage
$3,970,541
Filing date: 6/7/2004
Seller: Ryan Companies Inc.
Buyer: Rio Bravo LLC
Property ID: 263480010

2080 11th Av. E.
North St. Paul
$3,600,000
Filing date: 6/10/2004
Seller: GLP Investments LLC
Buyer: PMP Enterprises LLC
Property ID: 112922140004

1501 Hwy. 7
Hopkins
$2,350,000
Filing date: 6/15/2004
Seller: Swervo Development
Buyer: Mathwig Development Inc.
Property ID: 2411722220002
Property ID: 2411722220071
Property ID: 2411722220074

421 Lake Dr.
Chanhassen
$2,200,000
Filing date: 6/7/2004
Seller: Warm Water Ponds LLC
Buyer: Thomas Cloutier
Property ID: 258440010

13467 Business Center Dr.
Elk River
$1,990,003
Filing date: 6/8/2004
Seller: Larch LLC
Buyer: CK Star I LLC
Property ID: 755750105

21150 Rogers Dr.
Rogers
$1,900,200
Filing date: 6/15/2004
Seller: Jonathan Miner II LLC
Buyer: Myron Kujawa
Property ID: 2312023110001

1385 Mendota Heights Rd.
Mendota Heights
$1,725,000
Filing date: 5/12/2004
Seller: Cattail Realty LP
Buyer: Kong Khieu
Property ID: 274830007202
Property ID: 274830008002

2401 Chicago Av.
Minneapolis
$1,450,000
Filing date: 6/23/2004
Seller: Alef Co.
Buyer: Chicago Commons Corp.
Property ID: 3502924240001
Property ID: 3502924240003
Property ID: 3502924240004
Property ID: 3502924240007
Property ID: 3502924240008
Property ID: 3502924240009

3829 & 3901 Foss Rd.
St. Anthony
$1,350,000
Filing date: 6/17/2004
Seller: St. Anthony Village Properties
Buyer: Mirror Lake Properties LLC
Property ID: 313023410008
Property ID: 313023440042

401-409 Johnson St. NE.
Minneapolis
$1,332,500
Filing date: 6/3/2004
Seller: Mike's Fixture Co.
Buyer: Paloma Partners LLC
Property ID: 1302924430038

1206 114th Lane NW.
Coon Rapids
$1,120,000
Filing date: 2/13/2004
Seller: H&R Properties Inc.
Buyer: Martina Properties LLC
Property ID: 143124130007

Bruce Bisping/Star Tribune

Duane Lund, left, managing partner of the Geneva Organization, and Keith Sturm, center, and Michael Houge, both principals of Upland Real Estate Group, are marketing their real estate investments through the Internet.

FRACTIONS from D1

Deals can involve retail, offices, hotels or housing

"There are opportunistic groups involved in this industry only because they can be," Vitale said.

TICs usually go hand-in-hand with 1031 property exchanges, which allow investors who've sold commercial properties, whether farms or stores or apartment buildings, to reinvest the proceeds tax-free in other commercial properties.

Investors have 45 days to identify three potential replacement properties and 180 days in total to seal a deal that reinvests all of their proceeds. A third-party intermediary is also required to hold the money in trust until the deal closes.

Those choosing the 1031 route can either buy a whole property — Upland offers triple-net lease retail properties, which require tenants to take care of everything from maintenance to taxes — or they can turn to TICs and buy a piece of a bigger property.

Unlike many triple-net properties, which require the buyers to come up with their own financing, TICs are pre-packaged. The investors pay for their share and usually are promised returns of 7 to 10 percent annually, along with benefits such as depreciation and appreciation of the property, without much continuing effort on their part.

H. Thomas Dunck, Midwest regional manager in Chicago for Investment Property Exchange Services Inc., a 1031 intermediary firm, said most people had to actively manage their previous properties and they often are happy to take an easier role with a property exchange.

"Baby Boomers are now getting closer to retirement age and they want to avoid the infamous '3 Ts' — tenants, toilets and trash," Dunck said. "They want something a little more passive, an armchair type of investment."

The biggest advantages of TICs is that they allow investors with just a few hundred thousand dollars to defer capital gains taxes and get steady returns with a piece of a big, stable property, said Safe Harbor's Houge. Otherwise, they might be forced to buy a bargain-basement property to get the tax break, or maybe just be shut out altogether.

TICs also allow wealthier investors to diversify their holdings in several properties.

Safe Harbor's principals retain equity in each deal in lieu of most fees. "We have skin in the game," Houge said.

Internet sales model

Safe Harbor blends the financial acumen and property procurement skills of Lund with the sales and marketing and Internet knowledge of Houge and Sturm.

Among other positions, Lund was founding shareholder and a senior executive of the New York Stock Exchange-traded real estate investment trust First Industrial Realty Trust, which was involved in $800 million in real estate acquisitions. His Geneva Organization also offers TIC investments outside of Safe Harbor.

Houge and Sturm have been buying and selling Kentucky Fried Chicken, Walgreens, Blockbuster and other retail outlets in the Midwest since the early '90s.

They began to focus on an Internet sales model soon after they started Upland. It offers detailed deal information to time-pressured 1031 investors, who can do everything online up to a letter of intent.

Upland broadcasts about 5,000 e-mails to a network of brokers and investment advisers when it has a new property available. That model is now being applied to Safe Harbor.

Safe Harbor offers several types of real estate, from senior housing to retail complexes to industrial properties and hotels.

Investors can mix and match in the fashion of a mutual fund, Lund said.

The variety of offerings is unusual in the TIC market, as is Safe Harbor's focus on selling to brokers rather than securitizing the real estate and selling it through broker-dealers. Even though it is selling its TIC shares as real estate, Safe Harbor makes a point of complying with securities rules. Houge calls it a "belt and suspenders approach."

Wendell Maltby, Midwest regional manager of the California-based intermediary Starker Services Inc., said that while Safe Harbor is relatively new, Geneva and Upland are well-established brands in the Midwest.

Houge said about 25 percent of Safe Harbor's TIC clients are not 1031 exchangers, just investors looking for an alternative to the stock market. He added that the percentage of such clients is growing.

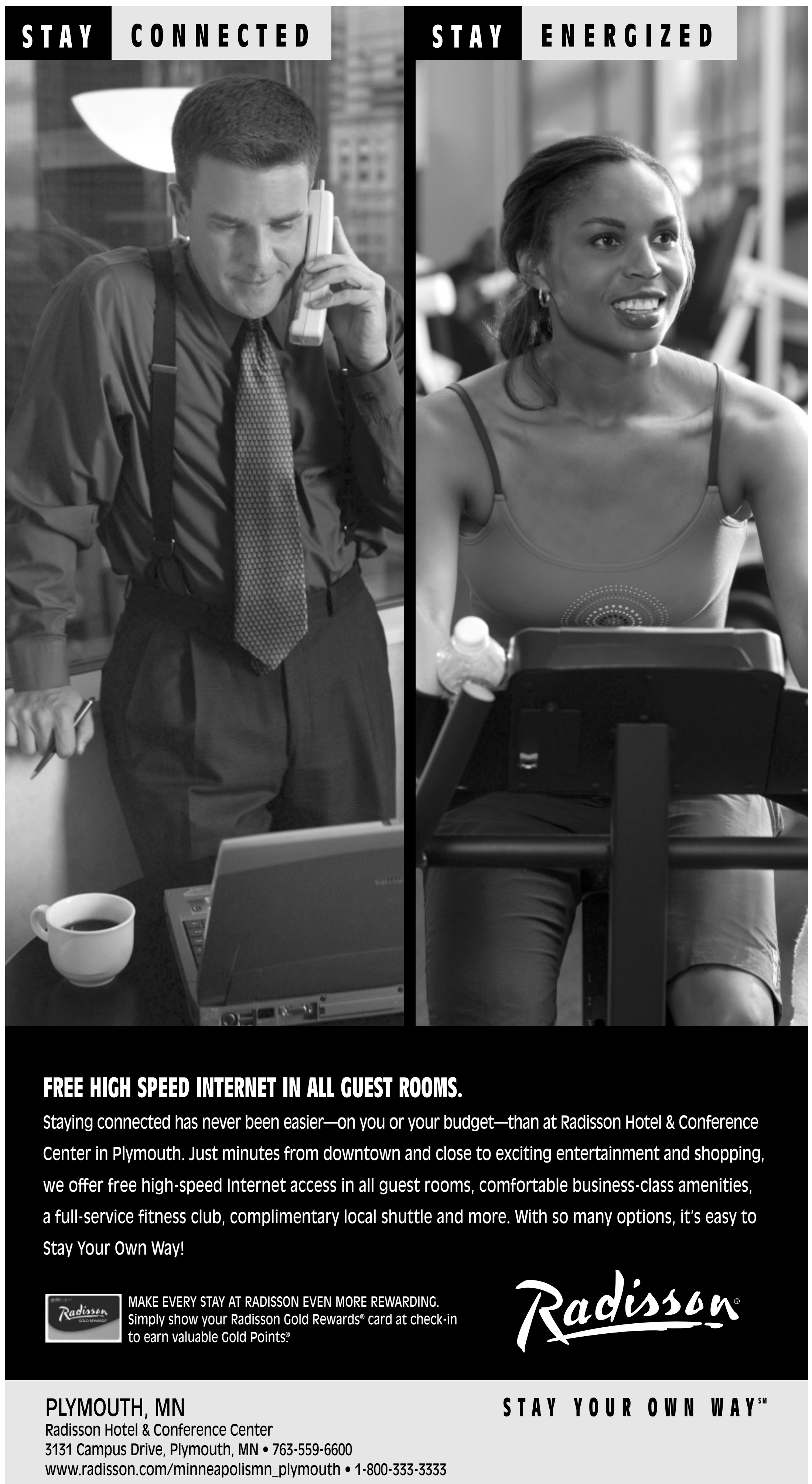
AEI's Vitale emphasized that investors should not let the "tax tail wag the investment dog."

"Everyone loves deferring taxes," Vitale said, "but in any TIC transaction you are engaging in a commercial real estate transaction and you have to make sure you have found real estate consistent with your return objective and your risk tolerance."

Houge said that even in the current go-go TIC market, the goal for Safe Harbor is simply to provide a stable and steady income flow from primarily Midwestern properties.

"We are not doing turnaround deals or swinging for the fences," he said.

Terry Fiedler is at tfiedler@startribune.com.



Copyright 2004 Star Tribune. Republished with permission of Star Tribune, Minneapolis-St. Paul. No further republication or redistribution is permitted without the written consent of Star Tribune