2018 FALL FORUM

Rising Leaders

Brightview Senior Living: Thriving through a combination of financing, development and management expertise

Over the course of a 36-year career built around one organization that initially financed, developed and managed multi-family housing before it saw an opportunity in 1996 to specialize exclusively in seniors housing, Marilynn Duker rose to CEO of Brightview Senior Living where she oversees 36 communities along the Eastern Seaboard with nearly 4,000 associates.

She looked back on her time with Brightview, traced the company's ascent and offered a glimpse at the future when she spoke during the 2018 Rising Leaders Fall Forum.

Brightview Senior Living got its start in Baltimore as The Shelter Group. First it developed multi-family properties, then managed approximately 25,000 units of market rate and affordable housing while also expanding into the investment and asset management business with an emphasis on tax exempt bonds.

One of the primary catalysts for the beginning of a transition from multi-family to seniors housing was the arrival of Arnie Richman, Brightview's chairman, in 1996. He was previously a partner in Meridian Healthcare, a large regional nursing home company that was acquired by Genesis HealthCare.

Combining Richman's health care and operations background with Brightview's finance and development experience led to a formidable force in seniors housing.

"For a number of years, we continued to develop and operate affordable housing, primarily for seniors, but we sold that 43-community portfolio in 2017 in order to focus 100 percent of our attention on our Brightview business. At that point, because of the growth of Brightview, the affordable business, was a small part of our overall business and we wanted to be able to focus our attention entirely on our senior housing business. It has turned out to be a great decision," Duker recalled.

Brightview's 36-community portfolio primarily consists of communities that are a rental continuum with independent living, assisted living and memory care.

Marilynn Duker, Brightview Senior Living

continued on page 2

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continued from page 1

Seven additional communities are under construction and will open during the next two years.

"We've chosen to develop the majority of our communities ourselves," she pointed out. "The last time we bought something was 2009, and we've learned we do better when we build our culture from the ground up. Our operations folks have a strong preference for that. It's very difficult to buy something and convert somebody else's culture to be your own. We've learned that from some pretty challenging experiences."

Brightview's capital structure revolves around a series of high net-worth equity funds. The four Brightview partners invest alongside the individuals participating in the funds to secure construction loans from banks and then in turn work with Fannie Mae and Freddie Mac for permanent debt.

"We wanted to be very long-term oriented and build a company that could go on way beyond the involvement of the four of us that currently own the business," she explained. "And we want to have the ability to operate the communities as we see fit without having a capital structure that forces us to make decisions about operations that we would not otherwise choose to make. We also want to grow in a very manageable, planful way.

"In large measure, we've been able to do just that. Our first fund that we raised in 1996 was only $5.8 million, and it was largely composed of friends and family. It took us four years to invest that fund, because we abandoned many of the sites that we had initially tied up due to concerns about overbuilding in the '90s.

"Each subsequent fund has been larger, culminating in our most recent and seventh fund, which was $200 million. We raised that in 2017. They've gotten easier to raise, coincidentally, as they've gotten larger. We have a tremendous amount of repeat investment and great word of mouth based on our track record. The four of us do all the fundraising ourselves, and I'm proud to say that one of the four of us knows almost every one of our now over 300 investors personally. This capital has been very patient and is structured to be long-term oriented. We have no obligation to ever sell any of the assets in our funds," Duker noted.

Individual investment in the funds ranges from $250,000 to $12 million. And in the most recent $200 million fund, Brightview employees contributed over $3 million. "We make that possible in a variety of different ways," she said.

"We have both matching funds and profits interests and with all these programs, there's some vesting associated with them," she continued, "so It's partly a retention tool. Then our most senior people invest right alongside the four of us and share pari passu with what we share in and receive."

The four Brightview partners invest a total of 10 percent in each fund, which added $20 million to the latest fund. But unlike many private equity funds where significant operator profits are derived from fees, Brightview has a lower fee structure and a somewhat more generous promote structure.

"If the funds do well, we do really well. But if they don't — and that's not been our experience — the investors are protected on the downside, because we haven't made a lot of money on fees, and we're right there with them," Duker said.

The Brightview capital structure emphasizes a conservative approach to underwriting by incorporating historic exit caps rather than the recent low rates. Brightview typically underwrites a more conservative loan-to-cost debt ratio than it is able to actually obtain. A 20 percent cushion is built into the projects' fill schedules.

"We've been incredibly fortunate to build long-term relationships with some terrific banks, many of whom continued to lend to us throughout the Great Recession, which enabled us to continue to grow during that time while a lot of other companies completely shut down their development operations," she commented.

"I attribute that in part to our conservative approach and the frequency and openness with which we communicate with our banks. We never surprise them with bad news," she said. "In the infrequent circumstance when we have an issue, we tell them early and we tell them often what's going on and what we're doing to correct it. We meet regularly throughout the year to communicate what we're doing to respond to the larger macro environment in the industry, as well as to share with them what we're doing to plan for growth."

While Brightview underwrites an internal rate of return in the mid-teens, to date, it has achieved significantly higher returns and multiples of two to 5.5 times equity. Duker credits rigorous risk management, a people-first operations strategy, combined with significant ongoing investments in the operating company that provide a very high level of support at the regional level for the communities in the portfolio for consistently delivering these results.

"We're highly selective about the sites and the markets in which we'll develop," she commented, "because we all know you can build the most beautiful buildings in the world with the latest bells and whistles, but if you don't have enough people and, more importantly, the right people to operate and oversee them, you're unlikely to be successful, and you may even have significant problems.

"We talk a lot in our company about how if you have highly engaged associates, you're much more likely to have highly satisfied residents, and if you have those two things, the financial results follow," she added.

During the last 20 years, after two major recapitalization transactions created an exit opportunity for investors, two new partnerships were formed that allowed Brightview to keep the assets in its portfolio and to maintain an ownership interest. Communities grouped in the two partnerships are operated in the same manner as the fund communities. "We've been fortunate to have terrific long-term oriented partners in PGIM and Harrison Street Real Estate Capital," said Duker.

Brightview over the last 10 years has opened two to four communities

annually and limits expansion to no more than five a year. "For every new community you open, you need 80 to 120 new associates. If you open five communities a year, that's 400 to 600 new associates a year that have got to be taught our culture," Duker said.

"We go to great lengths to ensure that we hire people who have the right values," she continued. "In addition to group interviews and multiple in-person interviews, we use personality assessment tools for management-level positions and another very intensive assessment tool for front-line associates. We also teach structured interviewing, particularly for front-line associates, that's behavior based, not experience based.

"Our executive directors interview every single person that's coming to work in their community. We invest a lot of time in teaching our approach to hiring. And we've got to do a really good job of on-boarding and training as well. That's something we're constantly working on and evolving. We're also making a big investment in leadership education and training for our next generation of leadership," she noted.

As part of the emphasis on preserving its culture, Brightview is actively engaged in succession planning to ensure continuity. "Given the age and maturity of our industry, this is going to be more of an issue over the next five to 15 years as a lot of the original founders in the industry get to a point where they need to transition out of their companies," Duker predicted.

"We felt it was important to get the succession plan started. So while we've built a lot of depth in the organization," she observed, "we didn't have anybody internally who had both the desire and the ability to step up to my role. In December 2016, we told everybody in the company that while I was not leaving the company or retiring, we were going to begin a process of recruiting a new President, which was then my title.

"We deliberately looked outside the industry. We were really fortunate to find Doug Dollenberg, who started with us about a year ago. He came most recently from the wireless technology industry after having worked at McKinsey for a number of years, so very far afield from

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continued on page 5

continued from page 4

senior living. But he had all the right leadership qualities and, most importantly, he was a great cultural fit," she said.

During a company orientation that provided an intensive introduction to senior living, Dollenberg spent four months in Brightview communities shadowing personnel in every role and then had a four-month immersion on the development and finance side of the business.

"We didn't immediately load him up with responsibilities," Duker said. "You never get that time back to develop a perspective on what we do well and what maybe we don't do that well. He developed a lot of credibility with the community teams, because he was with them day in and day out for months.

"We've used a modified version of that for a lot of different positions in our home office for a number of years now. It pays off in terms of allowing people to form their own perspective about how we do what we do before they're weighted down with day-to-day responsibilities. I promise you, if you try this approach once, you'll never go back. It's been invaluable," she stressed.

Duker believes that to succeed in the toughest labor market she can remember, it is imperative to hire from outside senior living.

"We've had great success with everybody from bankers to teachers to retailers. One of our best executive directors was a former regional manager at CVS, for example," she pointed out. "Always go with cultural fit over subject-matter expertise. You can teach people the substance of the business. Then give people the time and space to learn your business. They'll be more productive and add more value over time."

Stepping back to share her perspective on senior living's future, Duker singled out affordability and product innovation as two of the biggest issues facing the industry.

"Construction costs are escalating much more rapidly than five years ago," she observed, "so that inherently results in charging higher rates, therefore creating more risk as you open each new community. Certainly the Holy Grail for the industry would be finding a more affordable model for what we do.

"We need to think about our product as the consumer changes over the next 10 to 15 years. We recently opened our first two truly walkable, more urban-location senior living communities, and they've been very enthusiastically received. To some degree, the standard assisted living apartment is like the old nursing home used to be. That part of the product segment has to evolve somewhat in order to meet consumer demand, because it's becoming less desirable.

"Much of the market hasn't chosen senior living, in part because of the product. Understanding and listening to the 80 percent of the market that doesn't choose senior living is a real opportunity to increase penetration rates in the industry," she said.

While she acknowledges the potential for technology to extend the time seniors spend in their houses, Duker also sees limitations. "In an industry that's fundamentally built on relationships between our associates and residents, those efforts to keep people in their house are only going to be so successful, because technology's never going to overcome the isolation when you can no longer drive or get to see your friends," she pointed out.

continued from page 5

> “Wage escalation is in the four percent range.”

“Predictive analytics is very exciting in terms of the data that can be gathered and then used to predict and help reduce things like turnover, increase retention, predict possible resident care needs, track resident health and those kinds of things. So I’m really looking forward to seeing what that produces,” Duker commented.

Broader involvement in health care services is a looming opportunity, she contended, but this may take a while to play out. “We have one community that is very close to signing a deal with a local hospital, where the hospital would use us to help reduce their readmissions and to house people who need to some additional care, but they don’t need to be in a hospital setting.

“It’s taken more than a year to negotiate that deal. When you’re dealing with hospitals or health care systems, it’s incredibly bureaucratic and very slow-moving. It remains to be seen how well that works.

“We’ve certainly heard for years this expectation that somehow this is going to be a real boon to the industry. There’s definitely going to be opportunity there, but it’s going to be challenging, to deal with health care systems,” she said.

Finally, maintaining an engaged workforce in the face of an extremely competitive labor market will be paramount. “It’s definitely going to compress margins,” Duker stressed. “The industry in general hasn’t had to worry about expense control at all for basically its whole existence. Now we’re starting to see that for the first time, with wage escalation up in the four percent range.

“We’re all going to face it. We’re going to have to figure out whether we can recoup some of that in rate or whether it’s going to affect margins,” she added. ■

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