BOARD OF ASSESSMENT APPEALS, STATE OF COLORADO 1313 Sherman Street, Room 315 Denver, Colorado 80203 Petitioner: **EOP – TERRACE, LLC,** v. Respondent: **ARAPAHOE COUNTY BOARD OF EQUALIZATION.**	
Attorney or Party Without Attorney for the Petitioner: Name: Layne F. Mann, Esq. Address: 7475 West Fifth Avenue, Suite 321 Lakewood, Colorado 80226 Phone Number: (303) 233-8533 E-mail: Attorney Reg.: #15611	**Docket Number: 35515**

ORDER

THIS MATTER was heard by the Board of Assessment Appeals on June 29, 2001, Karen E. Hart and Mark R. Linné presiding. Petitioner was represented by Layne F. Mann, Esq. Respondent was represented by George Rosenberg, Esq.

PROPERTY DESCRIPTION:

Subject property is described as follows:

PART OF LOT 2 BLK 5 DENVER TECH CENTER
(Arapahoe County Schedule No. 2075-16-3-01-010)

Petitioner is protesting the 1999 actual value of the subject property, a multi-tenant office building situated at 5575 DTC Parkway, in the Denver Technological Center. The improvements consist of 115,408 net rentable square feet, situated on a site comprising 125,000 square feet. The building is configured with 3 stories, and was constructed of reinforced concrete in 1980. The property includes an adjacent parking garage constructed in 1985, that contains 108 covered parking spaces and 305 off-street surface parking spaces.

ISSUES:

Petitioner:

Petitioner contends that the best indicator of the subject's value is what the property would produce from a net operating income standpoint to an investor. The Petitioner relies on the actual income and expenses of the subject, as well as the actual vacancy. The cost and income approaches are addressed as well.

Respondent:

Respondent contends that there are two base year sales for the subject. Subject sales tend to be a strong indicator of value. The Respondent considered all three approaches to value. The market evidence from the direct sales comparison approach to value tends to provide a good indication of value. An income approach was also developed that provides additional support to the concluded value.

FINDINGS OF FACT:

1. Petitioner's witness, Jack P. Hanna II, Colorado Certified General Appraiser, presented the following indicators of value:

Market:	$10,617,536.00
Cost:	$ 9,708,585.00
Income:	$10,509,740.00

2. The witness testified with respect to the description of the subject property. The subject is known as the Terrace Office Building. The building contains a total 115,408 rentable square feet. The improvements are situated on an irregularly shaped parcel with 108 parking spaces. In addition to the on-site parking, there is additional off-street parking for 305 spaces. The subject is considered a Class B building, though it is surrounded by Class A buildings.

3. Petitioner's witness presented a cost approach to derive a market-adjusted cost value for the subject property of $9,708,585.00. The cost approach was based on data from Marshall & Swift Valuation Service, a state-approved cost data source. The witness testified that the cost analysis was utilized in his analysis, but due to age, the difficulty of estimating depreciation, and the lack of reliance on this methodology by the market, he placed no reliance on this approach.

4. The witness presented an income approach estimate of value of $10,509,740.00. The witness detailed the various data utilized in arriving at his income approach to value. He utilized a net rentable area of 115,409 square feet. This building area was taken from a rent roll that considered all of 1997 and the first 6 months of 1998. During the base period, the rental rate for the subject was $18.89 per square foot. The witness testified that he applied a 15.3% vacancy rate that was the average of the 1997 and 1998 data. The budgeted actual expenses, detailed on pages 22-24 of his appraisal report were $4.62 per square foot. The witness testified that no

actual 1997 and 1998 expense data was available given that the current ownership purchased the property after that time period. The witness testified that he also applied a 2% replacement reserve. Miscellaneous income from the parking garage was also added. The capitalization rate included property taxes. The base rate was 8.8%, with an effective tax rate of 3.46%, resulting in a concluded aggregate rate of 12.26%. The concluded capitalization rate was based on data from the American Council of Life Insurance (ACLI), and an analysis of comparable sales.

5. The witness testified that he placed the greatest weight on the income approach in his appraisal analysis. The witness testified that he believed that the county placed weight on the income approach as well. The witness testified that the income approaches in both the Respondent and Petitioner's appraisal reports were reasonably similar. The rent rate was quite similar, with a difference of only $.11 per square foot. Expenses were also very similar. The vacancy rate was taken from the actual performance of the subject; 15.3% was not typical for the market. The property continued to have a high vacancy rate into 2000.

6. The witness felt his capitalization rate was more indicative of the actual operating environment of the subject. The method the assessor used skews the data somewhat.

7. Mr. Hanna testified that the subject has a good location; but competes with very good quality buildings and does not have good visibility within the Denver Technological Center, though it does have good visibility from Interstate 25. The subject is next to a twin tower high rise that limits the visibility of the subject; the combination of the neighboring building and position from the subject parking garage and landscaping make it less desirable.

8. The witness testified with respect to the direct sales comparison analysis, concluding a value of $10,617,536.00. In the analysis for this approach, the witness testified that he used a qualitative adjustment process rather than quantitative analysis. Five comparable sales were utilized in the analysis. The comparable sales ranged from $82.07 to $102.97 per square foot. The sales that were determined to be most comparable were Sales #1, #2 and #3. He concluded $92.00 per square foot as the most appropriate valuation for the subject.

9. The witness testified with respect to the sales that had occurred involving the subject property. There were a total of two sales on the subject. The first sale occurred on July 1, 1997 for an indicated price of $13,190,000.00. The witness obtained information on this sale from the current owner. The purchaser thought that they could solve the excess vacancy impacting the subject in one to two quarters, or six months after the purchase. In actuality, it took two years to bring the property below 10% vacancy. Additionally, the subject property performed 27% below budgeted expectations.

10. With respect to the second purchase, the witness testified that this sale occurred in July 1998. The sales price of $15,000,000.00 was arrived at through an allocated value of a nine-property portfolio. The purchaser performed cash flow assumptions. The assumptions were performed in conjunction with the analysis of the remaining buildings, given the nature of Real Estate Investment Trust purchases; the witness felt it was indicative of an investment building and not of market value. The assumptions made by the purchaser were not achieved. One example was that the rental rate expectations were not made, and that a rate of $21.00 versus $20.00 was not achieved for the property as a whole.

11. Mr. Hanna testified with respect to the fact that a valuation allocation from a larger portfolio sale of nine properties was the basis of the subject's sales price.

12. The witness identified three articles that were contained within Petitioner's Exhibit A that were intended to identify Real Estate Investment Trusts (REIT). The witness testified that the articles discuss the relationship between value and sales prices as paid by REITs, and the fact that other items are considered besides current market value. The articles were intended to provide an understanding of the idiosyncrasies of the REIT market. REITs purchase on the basis of investment value rather than market value.

13. Mr. Hanna testified that the assessment in place for the subject for 1999/2000 was $12,500,000.00, and for 2001 was $13,250,000.00.

14. After considering all of the approaches to value, the witness testified that through his reconciliation of all three approaches he concluded a value for the subject of $10,500,000.00.

15. The witness testified under cross-examination that he did not know if the current property owner would sell the subject for $10,500,000.00.

16. The witness further testified that Class A properties sometimes have higher rental rates in comparison to properties in a lesser class.

17. Mr. Hanna testified that some purchases are made for investment purposes and equal market value, while some exceed market value.

18. Mr. Hanna explained that an REO was defined as Real Estate Owned. During bad times, savings and loans had to take properties back through foreclosure. When these properties were taken back, they were reported as sales. He further testified that these transactions could be used as sales in an appraisal, though one would have to be very careful in their use.

19. With respect to his cost approach analysis, the witness testified that the market approach is appropriate to use for vacant land. He used a land analysis, looking at what few land sales were available, and by additionally examining the land value concluded by the assessor. He admitted that he did not include a land analysis in the cost approach. His rationale for not including a land valuation analysis was that he placed no reliance on the cost approach.

20. The witness testified that the actual vacancy for the subject property in 1998 was 16%, and for 1997 the actual vacancy was 14%. The witness further testified that this rate was only for vacancy, and did not include collection loss factors.

21. The witness testified under cross-examination that the American Council of Life Insurance capitalization rates were more of a lender rate than a market rate.

22. The witness testified that he utilized a variety of source data in arriving at expenses for the subject. He did not have 1997 expense data, and felt that one could not simply double the half-year 1998 expense information. Expenses do not occur in a regular fashion. He relied on other data as well, including the Building Office Managers Association (BOMA) data. The pro-forma he prepared used actual data when possible; market data when necessary, given the fact that certain data was unavailable.

23. With respect to the direct sales comparison or market approach, the witness testified that though the sales utilized were somewhat older than the subject, the sales of this size and class tend to be somewhat older. He testified that each of the comparable sales was adjusted to net rentable area for comparative purposes. He made no adjustment for rent rates or occupancies. He developed his time adjustment through analysis of comparable sales. An annual rate of 12% was his conclusion, based on the data he examined. He felt that he might have been a little high in his time adjustment conclusion.

24. The witness admitted under cross-examination that Sale #3 and Sale #5 were also allocated sales prices. He felt that the portfolio sales he included as comparables were reflective of market value, while the portfolio sales that included the subject were not.

25. In redirect testimony, the witness indicated that he did his best to obtain actual base year expense data, noting that he asked the client for the information and was unable to obtain it. The current owner does forward-looking income analysis and does their own investigation, but they do not place much reliance on historical data.

26. He did not consider the expenses of the additional buildings included on the 1998 expense exhibit; he included the document in his exhibit precisely as it was included in the report provided to him by his client.

27. Petitioner is requesting a 1999 actual value of $10,500,00.00 for the subject property.

28. Respondent's witness, Mr. Corbin Sakdol, a Certified General Appraiser with the Arapahoe County Assessor's Office, presented the following indicators of value:

Market:	$14,900,000.00
Income:	$13,400,000.00

29. Based on the income and market approaches, Respondent's witness presented an indicated value of $14,150,000.00 for the subject property.

30. The witness testified that there were two sales on the subject property during the applicable base period. Sale #1 was at $13,190,000.00. Sale #2 was at an indicated price of $15,000,000.00.

31. The witness testified that he relied on Ross Research and Costar/Comps.Com for much of the data contained within his report.

32. With respect to Real Estate Investment Trusts (REITS), the witness testified that REIT's are most frequently interested in investment grade property; in areas such as the Denver Tech Center and downtown Denver marketplace. The witness felt that REITS are making the market in the DTC. Entities such as CarrAmerica, pension plans, and other institutional investors are all active in the same market.

33. Mr. Sakdol testified that the subject is a Class B building, and further indicated that the Ross Report data is broken down by class.

34. In the direct sales comparison approach, the witness testified that he examined and reviewed 30 sales, and utilized the six most comparable sales.

35. The witness testified that he adjusted Sale #1 (subject property) for personal property; $14,970,000.00; the sale was personally confirmed with the buyer. The witness testified that the buyer indicated that they analyzed the property and the purchase price reflected their belief of the property's value. The witness testified that Sale #2 was also of the subject. This sale took place on July 1, 1997. The sales price per square foot was $115.08. Sale #3 was of Richfield Plaza, at 5775 DTC Boulevard. The sale occurred in June of 1998. The sales price was $9,700,000.00. The indicated sale price per square foot is indicated as $81.44. This is an older property in comparison to the subject, having been constructed in 1974 versus the subject's 1980 construction date. Sale #4 was of the Quorum at DTC. This sale occurred in December 1997, with an adjusted sales price of $11,622,000.00. This is an older property that was constructed in 1975. The indicated sales price per square foot was $93.74. Sale #5 was of Orchard Pointe, which transacted in December 1996. The sales price was $13,525,000.00, which was adjusted by $28,644.00 of personal property, resulting in a sales price per square foot of $119.12. This property is somewhat newer than the subject, having been built in 1984. Sale #6 is of Yosemite Office Center. This property sold for $7,063,100.00 in June of 1997, with a sales price per square foot of $102.65.

36. If the subject sales were excluded, the remaining sales would support his estimate of value. He demonstrated for the Board an array of the sales, and commented that the subject falls squarely in-between the superior and inferior sales.

37. With respect to the differences between typical sales and REIT transactions, the witness testified that REIT purchases are placed on the open market. Buyers are fully aware of the nuances of the market, and REITs know how to analyze the properties and make a purchase decision. The witness commented that REITs are predominantly represented in these markets, and thus the sales from these markets should be used.

38. The witness testified that after applying appropriate adjustments to the comparable sales, a value per square foot of $130.00 was determined to be appropriate. Based on a consideration for all of the relevant data, the witness concluded a value of $14,900,000.00 from the direct sales comparison approach.

39. Respondent's witness did not apply the cost approach analysis in determining a value for the subject, indicating that it was not appropriate for this class of property, and the fact that investors did not consider the cost approach in their purchase decisions. The witness testified that the cost approach was considered, but he concluded that it would carry very little weight, and therefore did not include it in the appraisal report.

40. Respondent's witness used the income approach to derive a value of $13,400,000.00 for the subject property.

41. Mr. Sakdol testified that he was unable to obtain actual income information on the subject property, given that the owner said they were not available.

42. Given the unavailability of income and expense data, the witness testified that he relied on market-derived information. Through an examination of base-year rental negotiated leases, a rental rate of $19.00 was concluded. Market vacancy data was obtained from the Ross Report, and a concluded rate of 5.95% was derived. Derivation of expenses was based on a consideration of a variety of source data that aggregately provided support for the concluded expenses of $4.22 per square foot. The capitalization rate was derived through a consideration of extracted rates from actual market transactions for which the witness had developed a thorough study from properties that reported to the assessor. Reliance was also placed on Comps.com data that indicated a range of 6.61% to 9.54%. The subject itself had an extracted capitalization rate of 8.36% from the July 1998 sale. The average of the capitalization rates extracted from the sales transactions was 8.34%.

43. Under cross-examination, the witness testified that he did not know if Arapahoe County had a policy on the use of bulk sales. He indicated that he considered available sales as appropriate, and analyzed all sales data.

44. With respect to the subject sales, the witness testified that he did not feel that the sales were based on purely allocated values. If they had been, he would not have used the sales. Based on his discussions with Peter Kiff, a representative of the owner, taken in tandem with the sales assumption analysis the owner provided him, he felt that the sales price was supported.

45. With respect to the income analysis and his pro-forma analysis, the witness testified that he used vacancy from the market rather than the actual experience of the market, because he was not performing a leased-fee analysis, but rather, was performing a fee simple analysis.

46. Respondent assigned an actual value of $12,500,000.00 to the subject property for tax year 1999.

47. Petitioner’s witness Jack Hanna II testified in rebuttal with respect to the Respondent’s sales comparables. Comparable Sale #6 is 40% smaller in size, which is considered significant. He felt that a size adjustment would be appropriate.

48. The witness testified further on Sales Comparable #5. This sale occurred outside of the applicable base period. While you can do this when there are insufficient sales; he felt there were sufficient sales, and that this sale was only included because it represented a higher sales price per square foot.

49. Providing further explanation with respect to the subject sale, the witness testified that he was told the subject sales price was derived from pure allocation only.

50. The witness further testified that he felt the capitalization analysis was skewed, thus skewing the rate that was used because of the nature of the sales that were used. This included the inclusion of the subject sale.

51. With respect to the verification of the subject's sale by the assessor, Mr. Hanna testified that the individual verifying the sale was Mr. Kisluk, a representative of the subject property owner in the investor relations department. The witness questioned the in-depth knowledge that this person had of the actual sale.

52. The cash flow analysis he provided does not arrive at a valuation conclusion. It was part of a greater portfolio analysis.

CONCLUSIONS:

1. Respondent presented sufficient probative evidence and testimony to prove that the subject property was correctly valued for tax year 1999.

2. The Petitioner presented a cost approach to value, and though the derivation of the land valuation could have been more traditionally ascertained, the Board does not agree with the Respondent's assertion, contained on page 24 of Respondent's Exhibit #1, that the cost approach is "only a reliable indicator of value when the improvements are new, proposed, or special purpose." That the Petitioner was able to present such an approach is ample proof that such an approach can be quantified and applied to support the valuation conclusions of the direct sales comparison and income approaches to value.

3. While the Board agrees with the Petitioner that the sales on the subject may have various nuances that could potentially color their applicability, the Respondent is correct in asserting their applicability for consideration in this instance. There were two distinct sales transactions that occurred involving the subject, and the testimony presented offered conflicting viewpoints relating to the admissibility of the two sales into the valuation process. The Board concurs with the Respondent to the extent that the sales are reflective of institutional motivations for institutional grade properties such as the subject. The Board also concurs with the Petitioner that such sales may have other inherent considerations relating to the internal rationale of the purchaser in arriving at the sales price. It is interesting to note that the valuation assigned to the subject is below the value indicated by either the July 1997 sale price of $13,190,000.00 or the July 1998 sale price of $15,000,000.00. This appears to be demonstrable evidence that the Respondent did not place much weight on these sales transactions in the current assigned valuation. Having recognized both of these positions, the Board believes that while the sales

may be reasonable indicators of value for the subject within the direct sales comparison analysis, they are not by themselves sufficiently compelling to support a value greater than the $12,500,000.00 presently applied to the subject by the Respondent.

4. The Board believes both witnesses to be credible in the valuation indicators presented for its consideration. The data and analysis presented were credible from both parties, and the witnesses are to be commended for the clarity of their presentation and the depth of their research and analysis.

5. The Board notes that the valuation assigned by the Respondent is $12,500,000.00. The Petitioner presented evidence asserting a valuation of $10,500,000.00, and the Respondent presented evidence and a report concluding $14,100,000.00. The Board concludes that the valuation conclusions of the Petitioner give too great a weighting to the short-term vacancy. The Board has consistently considered the long-term vacancy over the economic life of a property, giving no consideration to short-term spikes in vacancy that may from time to time occur. Given the weighting given by the Petitioner to the income approach, the impact of the vacancy is such that it diminishes the final valuation conclusions. Similarly, the Board is not entirely persuaded by the valuation conclusions of the Respondent, in that too much weighting is given to sales that obviously were not weighted in concluding the current assigned value of $12,500,000.00.

6. The Board was most persuaded by the Respondent's income approach analysis. While both sides presented appropriate market-derived income data, they were also both hampered by the fact that historical information on the subject was not available. Due to this, both Petitioner and Respondent attempted to derive sufficient market evidence to supplement the lack of historic data. In the case of the Respondent, the data and analysis presented was exemplary. Even so, the Board notes that the overall valuation indications from this analysis, while well supported, appear to conclude a value at the higher-end of the indicated range of potential valuation outcomes.

7. In the end, the Board felt that the valuation conclusions of both parties were colored by their beliefs as to the applicability of the direct sales comparison data, the corresponding sales information during the base year, and the impact of excess vacancy during the applicable base period. Similarly, the income approach valuations of both sides, while diverging somewhat on several key components, presented a more reasonable measure of value. The main point of divergence was the application of a vacancy and collection loss allowance.

8. Based on the data presented, the Board believes that the current valuation assigned by the Respondent of $12,500,000.00 is appropriate and supported by the evidence presented.

<u>ORDER:</u>

The petition is denied.

APPEAL:

Petitioner may petition the Court of Appeals for judicial review within 45 days from the date of this decision.

If Respondent alleges procedural errors or errors of law by this Board, Respondent may petition the Court of Appeals for judicial review within 30 days from the date of this decision.

DATED and MAILED this 1st day of August, 2001.

BOARD OF ASSESSMENT APPEALS

Karen E Hart

Karen E. Hart

Mark R. Linné

This decision was put on the record

AUG 01 2001.

I hereby certify that this is a true and correct copy of the decision of the Board of Assessment Appeals.

Diane Von Dollen

Diane Von Dollen

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STATE OF COLORADO
SEAL
BOARD OF ASSESSMENT APPEALS