BOARD OF ASSESSMENT APPEALS, STATE OF COLORADO 1313 Sherman Street, Room 315 Denver, Colorado 80203 Petitioner: **GB 2 QUEBEC LLC,** v. Respondent: **ARAPAHOE COUNTY BOARD OF EQUALIZATION.**	**Docket No.: 66691**

ORDER

THIS MATTER was heard by the Board of Assessment Appeals on December 1, 2016, Diane M. DeVries and Gregg Near presiding. Petitioner was represented by Eric Steiner, Esq. Respondent was represented by Benjamin Swartzendruber, Esq. Petitioner is protesting the 2015 actual value of the subject property.

The parties agreed at the beginning of the hearing to the admission of Petitioner's Exhibits 1-12 and to Respondent's Exhibits A-E. Respondent provided a corrected page 58 to Exhibit A regarding the building size and identified another correction on page 55 for parking features on Comparable Sale 2. Respondent stated the corrections did not result in any changes to the value opinion(s).

Subject property is described as follows:

5600 S Quebec Street
Greenwood Village, CO 80111
Arapahoe County Parcel No. 2075-16-3-03-017

The subject is a free-standing Class B office building containing a net rentable area of 152,873 square feet built in 1976 on a 10-acre site. The building was designed with a central courtyard improved with trees and other landscaping. The structure is designed for multi-tenant occupancy.

Petitioner presented the following indicators of value:

Market:	$11,000,000
Cost:	Not applied
Income:	$10,646,212

Petitioner is requesting an actual value of $11,000,000 for the subject property for tax year 2015. Respondent assigned a value of $13,482,270 for the subject property for tax year 2015 and is submitting a site-specific appraisal for $13,500,000 in support.

Petitioner's witness, Mr. William Hybl Jr., President and COO of Griffis/Blessing Inc., testified regarding his company's purchase of the subject property in 2008. Mr. Hybl stated the purchase occurred at the high point in the market. After purchase the rental income declined and, as of the current date, lease rates are still not up to the 2008 levels. The witness recounted the subject's below average condition at the time of purchase pointing to significant maintenance expected to replace the roof, repair the parking lot and concrete and update the boilers and HVAC systems. Mr. Hybl compared the subject property to "the cheapest house in the neighborhood" as it was less attractive and the lowest cost in the market. The witness noted that a sister building was demolished for development of the Landmark project. The witness indicated the building has extensive parking which is a plus for office tenants and that one third of a three year plan to replace the asphalt and concrete had recently been completed.

Petitioner presented Ms. Dora Fessler, Portfolio Manager for Griffis/Blessing Inc. and the on-site manager for the subject building since 2014. Ms. Fessler testified in regard to the parking lot conditions and safety issues, noting she had already fallen three times in the lot. The witness referred to Exhibit 5, pages 2-19, the cash flow statements from December 2013 through June 2014, and to pages 20-28, the rent roll for the same period. Pages 31-37 are the end of year cash flow statements for 2014 and 2015. Ms. Fessler presented a summary of bids obtained in 2014 for repairs to the roof, parking lot and concrete totaling $1,467,832. Bids obtained in 2015 through 2016 indicate the current total would be slightly above that reported in 2014. The witness stated that annual maintenance is done on the roof but contractors all contend the roof needs to be replaced. Ms. Fessler indicated she would replace the roof today if given the go ahead by her manager.

Petitioner presented the final witness, Mr. Roger Bruhn, as an agent for the property owner. The witness stated he relied upon the information provided by CoStar. Arapahoe County records and reading *The Appraisal of Real Estate* published by the Appraisal Institute.

Petitioner's witness presented three comparable sales ranging in sale price from $5,310,000 to $13,550,000 ($61.07 to $68.96 per square foot of building area) and in size from 82,659 to 196,487. After adjustments were made, the sales ranged from $58.86 to $71.10 per square foot.

Mr. Bruhn adjusted the sales for features such as occupancy, location, condition, quality, size and date of sale. After averaging the three adjusted indications the witness concluded to a unit value of $62.97 per square foot. Mr. Bruhn then applied this unit value to the subject's building size of 172,493 square feet to conclude to an indicated value of $10,861,383 ($11,000,000 rounded). The witness testified that he accepted the information presented by CoStar without confirmation from any of the parties involved.

Mr. Bruhn presented an income approach to derive a value of $10,646,212 for the subject property. The witness adopted the average rent rate currently obtained and the size as stated by the owner. For 2014 the property generated $14.90 per square foot for 157.997 of net rentable area. No vacancy adjustment was applied as this figure is the actual rent. Mr. Bruhn adopted a projected 2015 income of $2,570,893 which reflects a base rental rate of $16.27 per square foot. After subtracting expenses of $1,662,340 the witness concluded to a Net Operating Income (NOI) of $908,553. To determine a capitalization rate the witness relied upon a survey of 19 buildings with reported cap rates. Rates within the survey ranged from 6% to 11.09% and the witness adopted 7.5% as appropriate. Application of a rate of 7.5% to the projected NOI for 2015 results in a value opinion of $12,114,044. This figure was then reduced by a charge for deferred maintenance of $1,467,832 resulting in a conclusion of $10,646,212 by the income approach. Noting the similarities between the conclusions of the two approaches applied, Mr. Bruhn reconciled to a final value of $11,000,000.

Respondent presented the following indicators of value:

Market:	$13,760,000
Cost:	Not applied
Income:	$13,465,000

Respondent's witness Mr. Mark Kane, a Certified General Appraiser, presented a market approach (sales comparison approach) containing three comparable sales ranging in sale price from $12,800,000 to $16,250,000 ($68.96 to $120.65 per square foot of building area) and in size from 134,691 to 196,487 square feet. After adjustments were made, the sales ranged from $82.75 to $108.58 per square foot.

Mr. Kane adjusted the sales for features such as location, size, parking and lot size. After consideration of the adjustments and the similarity of the sales to the subject, the witness concluded to a unit value of $90.00 per square foot. Mr. Kane then applied this unit value to the subject's rentable area of 152,873 square feet to conclude to an indicated value of $13,758,570 ($13,760,000, rounded).

Respondent's witness presented an income approach to derive a value of $13,465,000 for the subject property. Mr. Kane reviewed the subject's rent roll and determined an average contract rent as of 12/2013 of $16.40 per square foot of rentable area. Recent leases within the building ranged from $11.67 to $17.78/sf. The witness noted strong tenant loyalty with limited turnover evidenced by the rent roll. Analysis was also made of recent leases within competitive buildings in the market area, published statistics and the current asking rate of $19.00/sf full service for available space in the subject building. Mr. Kane adopted a rate of $17.00/sf. Other income from modified gross leases currently in place totaled $271,034 for 2013 and 2014; the witness applied a stabilized figure of $125,000. Occupancy in the subject building was 93% as of the valuation date while published sources were indicating vacancy rates from 11.6% to 12.7% to be common. Giving weight to both indications the witness adopted a stabilized vacancy rate of 10%. The witness analyzed the building expenses provided for 2013 and 2014 and, after separating them into typical categories, determined building expenses of $5.93/sf in 2013 and $6.63/sf in 2014. Adding an additional $0.50/sf for replacement reserves resulted in an expense rate of $6.50/sf. Published data supported a similar rate and Mr. Kane adopted $6.50/sf as appropriate for expenses. To determine a capitalization rate the witness considered the expected returns for alternative investments, multiple rates extracted from sales of suburban office buildings during the study period and rates developed by use of the Band of Investment and Debt Coverage Ratio. Ultimately, Mr. Kane concluded to a market capitalization rate of 7.5% which was increased by the Effective Tax Rate of 3.16% for an adjusted capitalization rate of 10.66%. Application of a rate of 10.66% to the projected NOI of $1,435,282 resulted in a value opinion of $13,464,188 ($13,465,000 rounded). Mr. Kane concluded to a final value of $13,500,000.

Respondent assigned an actual value of $13,482,270 to the subject property for tax year 2015 supported by a site specific appraisal report concluding to a value of $13,500,000.

Petitioner contends the subject property has significant deferred maintenance. The building was purchased at the top of the market in 2008 and immediate declines in rents caused repairs to the roof, parking lot and concrete to be put off long past the need for replacement. Any potential purchaser would discount an offer to purchase after recognizing the necessity to correct these deficiencies. As an alternative, the buyer might adjust the expected capitalization rate for this factor. Petitioner describes the subject as aesthetically inferior to the typical property in the market and the location is difficult to find. Petitioner asserts that Respondent has incorrectly focused on the size of comparable sales in the subject market area instead of considering buildings more similar in quality and condition.

Respondent contends Petitioner has failed to meet its burden of proof. Petitioner's agent has erred in his analysis of the building expenses, has failed to analyze comparable sales and leases from the market and, in the case of the market approach, applied inconsistent adjustments. Respondent argues Petitioner's agent has relied only upon the income information provided by the client and has incorrectly produced an opinion of the leased fee value instead of the required fee simple value.

The Board finds little merit in the value opinion provided by Petitioner. Petitioner's agent testified to no education in appraisal practice other than his reading of what was referenced, incorrectly, as the "handbook" of the Appraisal Institute. In presenting his opinion of actual value, Petitioner's agent stated multiple times that he did not confirm the data considered with any party to the transaction(s). The agent's comment that a Real Estate Owned (REO) transaction was equivalent to market value simply because the lender-owned property was exposed to the market contradicts the definition of market value and causes the Board to question the reliability of the witness's appraisal. The Board also rejects Petitioner's conclusion within the income approach finding that Petitioner incorrectly applied deferred maintenance and reserves for replacement. Petitioner's witness, Mr. William Hybl, in response to questions from the Board, clearly stated that it was not his practice to develop a reserve for replacement and, in his opinion, a 3% per year factor would be considerable. Petitioner's agent, in contrast, considered a replacement reserve of 12.6% of potential rent ($1.88 ÷ $14.90) to be appropriate (Petitioner's Exhibit 2, page 1). Both parties agreed that deferred maintenance was significant in the determination of actual value. Petitioner's Exhibit 2, page 1 provides insight regarding the process Petitioner's agent followed.

Using the subject's actual income, the agent presented a 2014 lease rate of $14.90/sf and subtracted $1.88/sf (12.6%) for Replacement Reserves. Later, under Operating Expenses, the agent indicates a stabilized reduction for "Capital Expenses" projected for 2015 to be $325,000, or, 12.6% of collected income. NOI for 2015 is therefore projected to be $908,553. This NOI is then capitalized at 7.5% to determine a value opinion of $12,114,044. The value opinion is then reduced by $1,467,832 for the estimated costs to repair the roof, parking lot and concrete. The final value opinion of $10,646,212 is unsupportable for the following reasons: (all on page 1, Petitioner's Exhibit 2):

- NOI applied is based on actual income without supporting research and analysis that the actual income is equal to market income.
- Projected income for 2015 is $2,570,893, or, $16.27/sf. This is an unsupported increase of nearly 9%.
- "Capital Expenses" of $325,000 are projected. This is equal to 12.6% of collected income, over 4 times the amount considered appropriate by Petitioner's witness (Mr. Hybl). The Board notes that at that level of contribution it will only take slightly more than 4.51 years to collect $1,467,832.
- A subtraction of $1,467,832 for deferred maintenance ignores previous expenditures of $292,029 (Petitioner's Exhibit 5, pages 33 and 37) reported as "Capital Expenses" for parking lot/garage.
- By burdening the property with a reserve ratio of 12.6% per year and then applying an "across the board" adjustment for deferred maintenance, the Board finds Petitioner's agent has adjusted twice for the same condition. *See* Appraisal of Real Estate, 14th Edition, pp. 484-487 (A reconstructed operating statement represents an opinion of the probable future net operating income of an investment. Certain items included in operating statements prepared for property owners should be omitted in reconstructed operating statements prepared for appraisal purposes. [. . .] *Expenditures for capital improvements usually do not recur annually and therefore should not be included in an estimate reflecting the typical annual expenses of operation*). Emphasis added.

Overall the Board has no confidence in the analysis presented by Petitioner's agent. Petitioner presented insufficient probative evidence and testimony to prove that the subject property was incorrectly valued for tax year 2015.

ORDER:

The petition is denied.

APPEAL:

If the decision of the Board is against Petitioner, Petitioner may petition the Court of Appeals for judicial review according to the Colorado appellate rules and the provisions of

Section 24-4-106(11), C.R.S. (commenced by the filing of a notice of appeal with the Court of Appeals within forty-nine days after the date of the service of the final order entered).

If the decision of the Board is against Respondent, Respondent. upon the recommendation of the Board that it either is a matter of statewide concern or has resulted in a significant decrease in the total valuation of the respondent county, may petition the Court of Appeals for judicial review according to the Colorado appellate rules and the provisions of Section 24-4-106(11), C.R.S. (commenced by the filing of a notice of appeal with the Court of Appeals within forty-nine days after the date of the service of the final order entered).

In addition, if the decision of the Board is against Respondent, Respondent may petition the Court of Appeals for judicial review of alleged procedural errors or errors of law within thirty days of such decision when Respondent alleges procedural errors or errors of law by the Board.

If the Board does not recommend its decision to be a matter of statewide concern or to have resulted in a significant decrease in the total valuation of the respondent county, Respondent may petition the Court of Appeals for judicial review of such questions within thirty days of such decision.

Section 39-8-108(2), C.R.S.

DATED and MAILED this 21st day of December, 2016.

BOARD OF ASSESSMENT APPEALS

Gregg Near

Diane M. DeVries

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

Milla Lishchuk

STATE OF COLORADO
SEAL
BOARD OF ASSESSMENT APPEALS

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