BOARD OF ASSESSMENT APPEALS, STATE OF COLORADO 1313 Sherman Street, Room 315 Denver, Colorado 80203 Petitioner: **PMT PARTNERS XIV LLC,** v. Respondent: **DOUGLAS COUNTY BOARD OF EQUALIZATION.**	**Docket No.: 67193**

ORDER

THIS MATTER was heard by the Board of Assessment Appeals on March 31, 2016, Sondra Mercier and MaryKay Kelley presiding. Petitioner was represented by John K. Dorwart, Esq. Respondent was represented by Meredith P. Van Horn, Esq. Petitioner is protesting the 2015 actual value of the subject property.

Subject property is described as follows:

7437 Village Square Drive, Castle Rock, CO **Sch. No. R0422463**
361 Village Square Lane, Castle Rock, CO **Sch. No. R0422457**
363 Village Square Drive, Castle Rock, CO **Sch. No. R0422461**

The subject property is a 3.6 acre commercial site (includes 0.486 acre of common parking) consisting of three buildings. The complex, known as Village Square, is located mid-distance between Castle Rock and C-470 and west of I-25 on the south side of Castle Pines Drive. Neighboring commercial centers include office buildings, a retail complex anchored by King Soopers, a retail complex formerly anchored by the now-vacant Safeway, and a Walgreens. The subject buildings are described as follows:

<u>7437 Village Square Drive (Sch # R0422463)</u> 15,812 gross sq.ft. 12,408 rentable sq.ft.
This two-story structure is comprised of main floor retail and second-floor office space built in 2001. One tenant, the tax-exempt Douglas County Library, will vacate this year and be replaced; the library's square footage is included in the valuations of both parties.

<u>361 Village Square Lane (Sch # R0422457)</u> 13,650 gross sq.ft. 13,156 rentable sq.ft.
One-level retail built in 2001.

363 Village Square Drive (Sch # R0422461)   25,476 gross sq.ft.   24,040 rentable sq.ft.
One-level retail built in 1998.

Respondent assigned a value of $2,100,000 to 7437 Village Square Drive, which is supported by an indicated value of $2,250,000. Respondent assigned a value of $2,593,500 to 361 Village Square Lane but is recommending a reduction to $2,400,000. Respondent assigned a value of $3,170,000 to 363 Village Square Drive which is supported by the indicated value of $4,100,000. Petitioner valued the complex as an independent entity and is requesting a total value of $5,900,000.

Petitioner presented the following indicators of value:

Market:	$5,985,000
Cost:	N/A
Income:	$5,830,000

Petitioner's witness, David G. Berger, Property Tax Consultant and Principal of R.H. Jacobson & Company, identified and valued the three buildings as one unit, arguing that they were owned by the same party, built as a commercial center, and shared parking.

Mr. Berger presented a Market Approach for the three-structure complex with four comparable sales ranging in sale price from $4,692,000 to $5,500,000. Adjustments were made for gross building area, land size, site access and visibility, construction quality, and age. After adjustments were made, the sales ranged from $5,541,675 to $6,341.350. Mr. Berger concluded to an indicated value of $5,985,000 for the complex.

Mr. Berger presented two Income Approaches, each including stabilized income of $1,065,000 and his analysis of actual income, contract rents, common area reimbursements (CAM), reimbursed tax expenses, and miscellaneous income. He considered these rents to be supported by market research (CBRE Research and Newmark Grubb Knight Frank). Mr. Berger noted that the center operated under net leases with one exception, that being Duke's Restaurant, whose gross lease was included in his calculation of stabilized income.

First Analysis: Mr. Berger's first analysis did not include taxes as an expense. Rather, the capitalization rate included an Effective Tax Rate (mil levy times the assessment rate of 29%). Expenses totaled $345,000 for a Net Operating Income of $720,000.

Second Analysis: The second analysis included taxes as an expense for a total of $575,000 and a Net Operating Income of $490,000.

Mr. Berger applied a capitalization rate of 8.5% based on the following: the Real Estate Investment Survey (Summer 2014) indicating a range from 7% to 10% and an average of 8.25%; and rates for his four comparable sales (Market Approach) ranging from 7.5% to 10% for an average of 8.9% and a median of 9%. He applied a tax load of 3.71% in his first analysis for a capitalization rate of 12.21%, which indicated a value of $5,896.606. His second analysis concluded to $5,764,706 based on an unloaded capitalization rate of 8.5%.

Mr. Berger assigned more weight to the Income Approach and reconciled to a value for the complex at $5,900,000.

Respondent's witness, Stephen M. Snyder, Certified General Appraiser for the Douglas County Assessor's Office, considered each of the subject buildings to be independent entities; each carried a separate schedule number; and each can be marketed separately. He presented the following indicators of value:

	361 Village Square Ln	363 Village Square Dr	7437 Village Square Dr
Mkt:	$2,573,500	$4,585,440	$2,356,760
Cost:	N/A	N/A	N/A
Inc:	$2,360,000	$4,095,000	$2,250,000

Mr. Snyder presented a Market Approach for each of the properties, using the same four comparable sales which ranged in sale price from $1,600,000 to $3,750,000. He made qualitative adjustments, deriving adjusted prices per square foot. He gave most weight to Sales Three and Four and concluded to $190 per square foot, which he multiplied by the square footage of each of the buildings to arrive at the above-stated conclusions.

Mr. Snyder presented an Income Approach for each of the buildings. An analysis of base period leases within the subject property compared to rents in other comparable retail properties was considered. A comparison of asking and starting rents for comparable retail properties suggested that a factor of 86.30% be applied to asking rents to adjust to actual market rents. He placed most weight on the starting rent at 556 Village Square Lane, which was $17.50 without adjustment.

Mr. Snyder researched the marketing area's vacancy rate at mid-year 2014 in a study of 116 retail buildings in Douglas County by CoStar (average rate of 10.7%) and applied a stabilized rate of 10%.

Mr. Snyder deducted 8% for non-reimbursable expense, with consideration given to the buildings' ages and overall condition.

Mr. Snyder applied a capitalization rate of 8% based on the following: Market Extraction (CoStar search of retail building sales in the metropolitan area resulting in a mean of 7.27% and a median of 7.25% and Douglas County sales resulting in an average of 7.32% and a median of 6.88%); and the Investor Survey Method (several published reports indicate a mean of 8.07% and a median of 8%). An overall rate of 6% to 10% was supported, and Mr. Snyder reconciled to a capitalization rate of 8% based on an opinion that the subject buildings were of good quality and in a good location.

Mr. Snyder did not consider 361 Village Square Lane and 363 Village Square Drive to be at stabilized occupancy on the date of value. He, therefore, made deductions for the cost of attaining stabilized occupancy; loss of rent, holding costs, leasing commissions, and tenant improvement allowance ($20,000 and $255,000 respectively).

Mr. Snyder concluded to the following stabilized values within the Income Approach: $2,360,000 (361 Village Square Lane); $4,095,000 (363 Village Square Drive); and $2,250,000 (7437 Village Square Drive).

Mr. Snyder placed greater weight on the Income Approaches and reconciled to the values indicated in that approach.

Petitioner presented sufficient probative evidence and testimony to prove that the tax year 2015 valuation of the subject property was incorrect.

The subject has an inferior location, with little frontage, difficult access, low visibility, and limited population in the surrounding area. Vacancy within the subject is reportedly high, trending at 15% to 25%, and is expected to increase when the library and judicial offices vacate, a fact known as of the date of value. Statistically, the vacancy rate in the surrounding retail area was high, and included a vacant Safeway that is located in a center that offers greater exposure and access than the subject. Respondent gave inadequate consideration to these factors in their valuation of the subject.

Respondent contends that each property must be valued separately citing Section 39-5-104, C.R.S., "Each tract or parcel of land and each town or city lot shall be separately appraised and valued, except when two or more adjoining tracts, parcels, or lots are owned by the same person, in which case the same may be appraised and valued either separately or collectively." The Board finds that on the assessment date, the properties shared common ownership, required cross access for parking and interior traffic, and were located in the same tax area. Further, both parties considered a fourth parcel that was not part of the appeal as necessary to meet parking requirements for the property overall.

After consideration is given to the three approaches to value, the Board finds the Income Approach to be the best indicator of value. Petitioner presented an Income Approach that reflected the actual income and operating expenses associated with the subject, essentially providing a value of the leased fee interest. Values for tax purposes must be market driven to reflect the fee simple interest, which was provided by Respondent; however, the Board finds that Respondent gave inadequate consideration to numerous functional issues associated with the subject. These issues can be addressed on a variety of levels within the Income Approach, including (but not limited to) reduced rent, above market vacancy, and/or higher capitalization rate.

Respondent concluded to a rental rate of $17.50 per square foot, net of expenses. This rate was at the lower end of Respondent's indicated range and within the range indicated by Petitioner's market information. A rate of $17.50 per square foot is supported, resulting in potential rental income of $868,070.

Petitioner added actual expense reimbursements received as additional income. Consequently, this methodology reflects actual vacancy for the subject on an annual basis, further leading to a leased fee value. Respondent's deduction of 10% for vacancy does not accurately reflect the locational issues of the subject that lead to above market vacancy and, subsequently, the high expenses paid by the owner because of that vacancy. Generally, all expenses with the exception of those identified as "owner's expense" are reimbursed by the tenants. Petitioner deducted $575,000 for expenses including $100,000 in owner's expenses for vacant units. The Board adds an additional $475,000 as potential reimbursable expenses ($9.58/sf) to derive potential gross income of $1,343,070 ($27.08 sf). The Board notes that Respondent's lease-up analysis identifies slightly higher building expenses of $10.00 per square foot for the subject.

Respondent applies a market supported vacancy and credit loss deduction of 10%. Respondent identified actual vacancy of 15% as of June 30, 2014. Petitioner reported that over the past 6 years vacancy had typically ranged from 15% to 25% and actual vacancy was 21% as of the statutory date of value. As previously discussed, locational issues of the subject can be reflected in an above market vacancy rate. The Board will make a deduction of 20% to reflect the owner's costs associated with vacancy issues.

Care should be given in determining the appropriate deduction for owner's expenses. Petitioner made a large deduction of $100,000 or $2.02 per square foot for owner's expenses. Respondent based their deduction on a more typical appraisal practice as a percentage of income, concluding to 8% ($1.26/sf) from a range of 3% to 8%. To better reflect the fee simple value of the subject, the Board concludes to a market supported deduction of 8% or $1.26 per square foot for owner's expenses.

The parties presented a tight range of capitalization rates, with Petitioner concluding to 8.5% and Respondent utilizing 8.0%. In one scenario, Petitioner applied a 12.21% rate inclusive of a tax load of 3.71%. The data presented by both parties indicates a wide range; however, the Board will rely on Petitioner's rate as more reflective of the issues facing the subject property such as location, poor visibility, and high historical vacancy.

Rentable Square Footage	49,604	
Rental Income	$17.50/sf	$868,070
Expense Reimbursement	$9.58/sf	$475,206
Potential Gross Income		$1,343,276
Market Vacancy and Collection Loss	10%	($134,328)
Vacancy from Functional Issues	10%	($134,328)
Effective Gross Income		$1,074,620
Less: Operating Expenses	$9.58/sf	($475,000)
Less: Owner's Expense	$1.26/sf	($62,501)
Net Operating Income		$537,119
Capitalization Rate	8.5%	$6,319,047
Rounded		$6,320,000

The Board concludes that the 2015 actual value of the subject property should be reduced to $6,320,000.

ORDER:

Respondent is ordered to reduce the 2015 actual value of the subject property to $6,320,000.

The Douglas County Assessor is directed to change his/her records accordingly.

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 25th day of May, 2016.

SEAL

BOARD OF ASSESSMENT APPEALS

Sondra W. Mercier

Sondra W. Mercier

MaryKay Kelley

MaryKay Kelley

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

Milla Lishchuk