

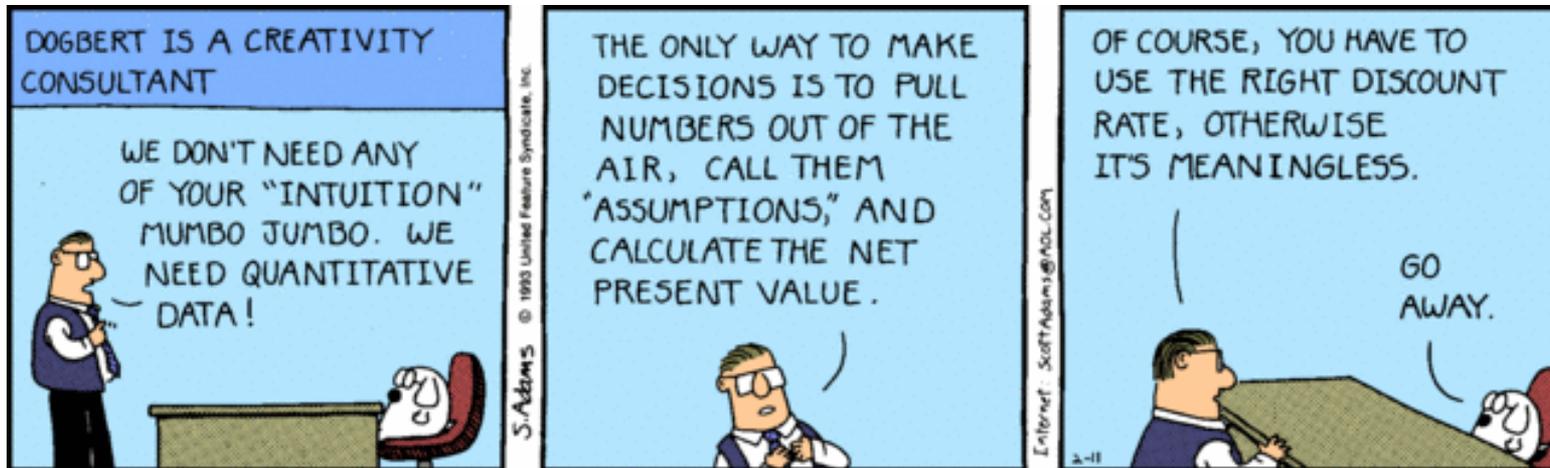
EFFECTIVE VS. CONTRACT RENT

Summer Seminars 2018



WHY ARE WE HERE?

- Petitioners use effective rent arguments in Tax Court negotiations and we need to be able to understand the methodology and the theory behind effective rent to properly apply it.



LEARNING OBJECTIVES

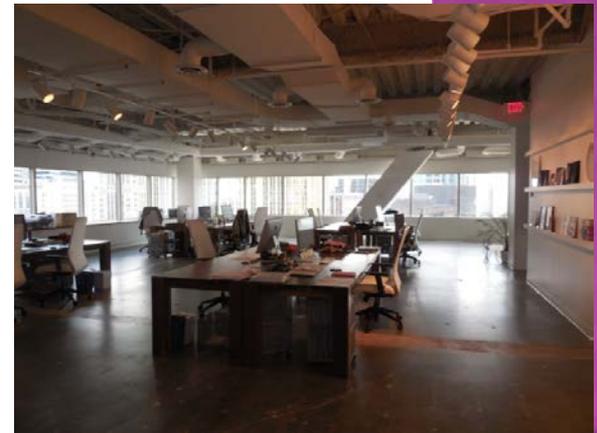
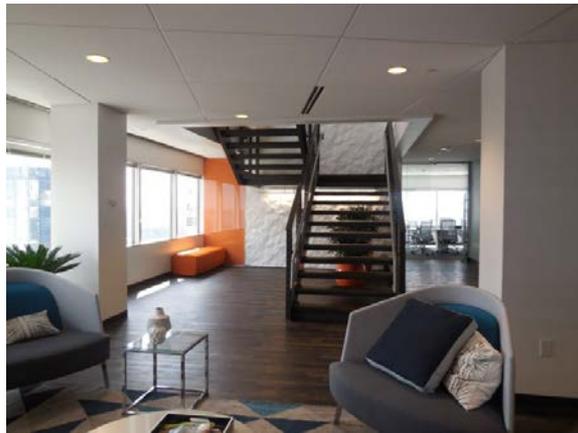
- ◉ Understand definitions relating to effective rent
- ◉ Recognize and understand the relationship between contract rent, effective rent and market rent
- ◉ Calculate effective rent with the three methods
- ◉ Applying effective rent to the three approaches to value
- ◉ Review Tax Court Decisions

WHAT IS EFFECTIVE RENT?

- “The total base rent, or minimum rent stipulated in a lease, over the specified lease term minus rent concessions; the rent that is effectively paid by a tenant net of financial concessions provided by a landlord.”

WHAT IS A CONCESSION?

- "2. An inducement for a tenant to lease space, sometimes, but not always, observed in overbuilt markets, which can include above-standard tenant improvements, free rent, moving cost reimbursement or credit, and buyout of the tenant's existing lease. Concessions are an integral part of the definition of market rent."



WHAT IS MARKET RENT?

- “The most probable rent that a property should bring in a competitive and open market reflecting the conditions and restrictions of a specified lease agreement, including the rental adjustment and revaluation, permitted uses, use restrictions, expense obligations, term, concessions, renewal and purchase options, and tenant improvements (TIs).”

CONCESSIONS - SOMETHING BEING GIVEN AWAY FOR FREE?

○ Examples

1. Start-up company needs office space but doesn't have the capital now to pay rent now. Landlord gives free rent at the beginning of the lease but charges more rent over the term of the lease.
2. Tenant doesn't have the funds to pay for above-standard TIs out-of-pocket. Landlord pays for the above-standard TI and charges more rent to cover the costs of the build-out

MARKET CONDITIONS

- The difference between contract rent and effective rent is often a function of market conditions.
 - When the market is strong and highly competitive, the difference is less.
 - When the market is soft and there is less competition, the difference is greater.

MEASURING EFFECTIVE RENT

○ Three methods

- Straight-line - Total rent paid over the lease term (less the landlord's out-of-pocket costs of the concessions) divided by the lease term.
- Modified Straight-line - Same as the straight-line, except the landlord's out-of-pocket costs are amortized at the landlord's cost of capital.
- Level-equivalent - Present value of the landlord's out-of-pocket costs and the value of the concessions plus the present value of the scheduled contract rents. Then the present value is amortized over the life of the lease at a discount rate.

WHAT IS TIME VALUE OF MONEY

- "The concept underlying compound interest that holds that \$1 (or another unit of currency) received today is worth more than \$1 (or another unit of currency) received in the future due to opportunity cost, inflation, and the certainty of payment."



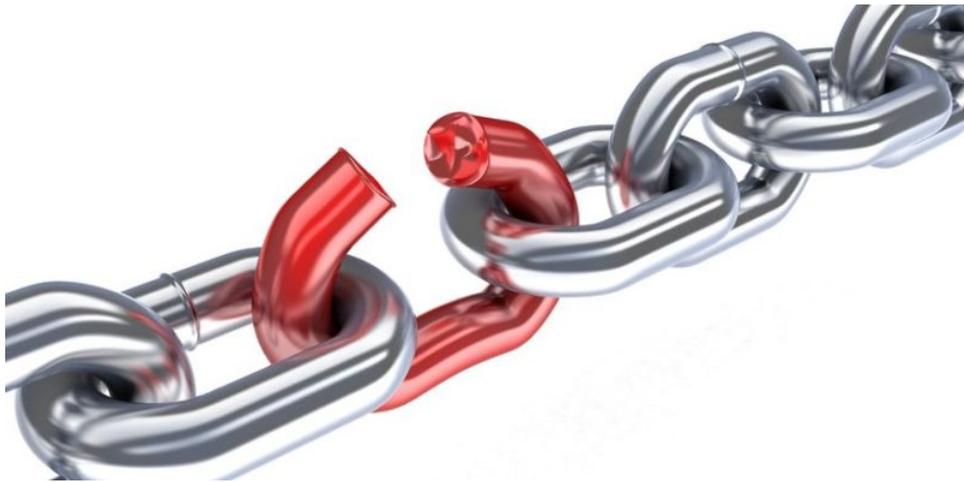
STRAIGHT-LINE METHOD

- Most simple to understand and explain
- Steps
 - Step 1 - Calculate the total contract rent that is received over the life of the lease
 - Step 2 - Subtract the sum of the value or cost of the landlord concessions
 - Step 3 - Equals effective rent (needs to be divided by the lease term)

STRAIGHT-LINE METHOD

○ Weaknesses

- Time value of money is not accounted
- Possibility of the landlord financing some of the concessions (also time value of money)



STRAIGHT-LINE METHOD

○ Steps

1. Calculate the total rent
2. Subtract free rent
3. Subtract excess TIs
4. Divide by the term

STRAIGHT-LINE METHOD

EXAMPLE 1

○ Example

- What is the effective annual rent per square foot for the following lease (using straight-line method)
 - Contract rent / year: \$20 per square foot
 - Lease term: 10 years
 - 10 months free rent, earned one month per year
 - No excessive TIs

MATH.

The only place where
people buy 60 watermelons
and no one wonders why.

STRAIGHT-LINE METHOD

EXAMPLE 1

○ Example

- Contract rent / year: \$20 per square foot
- Lease term: 10 years
- 10 months free rent, earned one month per year
- No excessive TIs

Calculate Total Rent = \$20 psf x 10 years = \$200.00

Subtract Free Rent = (10 / 12) x \$20 psf = -\$16.67

Equals = Total rent less Free Rent = \$183.33

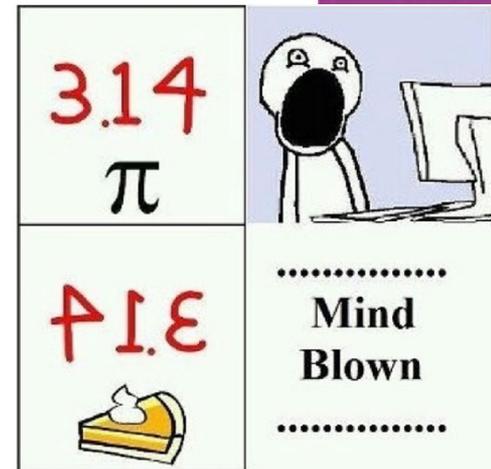
\$183.33 / 10 years = \$18.33 psf

STRAIGHT-LINE METHOD

EXAMPLE 2

○ Example

- What is the effective annual rent per square foot for the following lease (using straight-line method)
 - Contract rent / year: \$14 per square foot
 - Lease term: 5 years
 - 5 months free rent, earned one month per year
 - \$5 per square foot of excess TIs over market



STRAIGHT-LINE METHOD

EXAMPLE 2

○ Example

- Contract rent / year: \$14 per square foot
- Lease term: 5 years
- 5 months free rent, earned one month per year
- \$5 per square foot of excess TIs over market

Calculate Total Rent = \$14 psf x 5 years = \$70.00

Subtract Free Rent = (5 / 12) x \$14 psf = -\$5.83

Equals = Total rent less Free Rent = \$64.17

Less excess TIs -\$5.00

Equals \$59.17

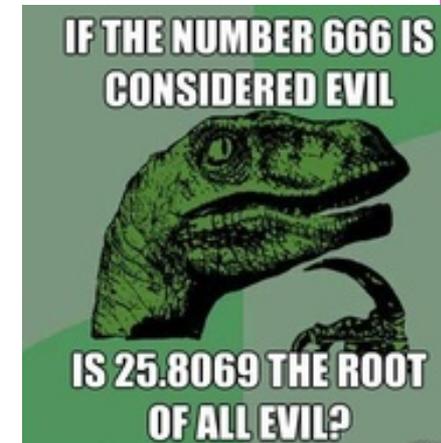
\$59.17 / 5 years = \$11.83 psf

STRAIGHT-LINE METHOD

EXAMPLE 3

○ Example

- What is the effective annual rent per square foot for the following lease (using straight-line method)
 - Contract rent / year: \$10 per square foot
 - Lease term: 4 years
 - 4 months free rent, earned one month per year
 - \$5 per square foot of excess TIs over market



STRAIGHT-LINE METHOD

EXAMPLE 3

○ Example

- Contract rent / year: \$10 per square foot
- Lease term: 4 years
- 4 months free rent, earned one month per year
- \$5 per square foot of excess TIs over market

Calculate Total Rent = \$10 psf x 4 years = \$40.00

Subtract Free Rent = (4 / 12) x \$10 psf = -\$3.33

Equals = Total rent less Free Rent = \$36.67

Less excess TIs -\$5.00

Equals \$31.67

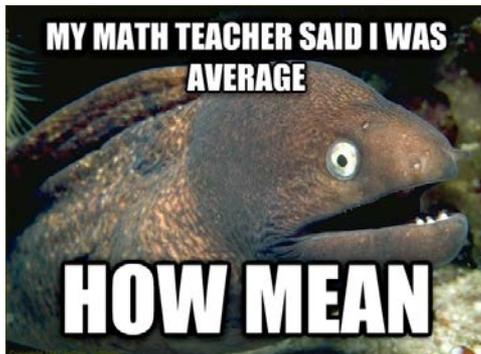
\$31.67 / 4 years = \$7.92 psf

STRAIGHT-LINE METHOD

EXAMPLE 4

○ Example

- What is the effective annual rent per square foot for the following lease (using straight-line method)
 - Contract rent: Starting at \$20.00 per square foot (\$0.50 annual increases)
 - Lease term: 4 years
 - 4 months free rent, earned one month per year
 - \$5 per square foot of excess TIs over market



STRAIGHT-LINE METHOD

EXAMPLE 4

○ Example

- Contract rent / year: \$20 per square foot (\$0.50 annual increases)
- Lease term: 4 years
- 4 months free rent, earned one month per year
- \$5 per square foot of excess TIs over market

Year 1 - \$20.00 psf x (11/12) =	\$18.33
Year 2 - \$20.50 psf x (11/12) =	\$18.79
Year 3 - \$21.00 psf x (11/12) =	\$19.25
Year 4 - \$21.50 psf x (11/12) =	\$19.71
<hr/>	
Total	\$76.08
Less excess TIs	-\$5.00
<hr/>	
Equals	\$71.08

$$\$71.08 / 4 \text{ years} = \$17.77 \text{ psf}$$

MODIFIED STRAIGHT-LINE METHOD

- Very similar to the Straight-line Method, but it addresses the issue of possible lessor financing of the tenant concessions.

MODIFIED STRAIGHT-LINE METHOD

- Weakness

- Does not address Time Value of Money

MODIFIED STRAIGHT-LINE METHOD

◉ Steps

1. Calculate the total rent
2. Subtract free rent
3. Divide by the term to get the annual rent net of free rent
4. Calculate the annual payment on the TI loan
5. Subtract the annual payment

MODIFIED STRAIGHT-LINE METHOD

EXAMPLE 5

- Suppose that in addition to free rent, the landlord borrowed money to provide Tenant Improvement Allowances of \$15 above what the market normally requires. The amount borrowed was amortized at 5.0% interest over a seven-year term (the term of the lease).

Parallel lines

have so much in
common...



it's a shame
that they'll never
meet.

MODIFIED STRAIGHT-LINE METHOD EXAMPLE 5



MODIFIED STRAIGHT-LINE METHOD

EXAMPLE 5

- ◉ Calculate the monthly payment for this loan.
 - ◉ Present value (PV) = \$15 psf
 - ◉ Number of periods (n) = 7 years (84 months)
 - ◉ Interest Rate (i) = 5.0% / year (0.42% / month)
 - ◉ Future Value (FV) = Nothing

 - ◉ Payment (PMT) = \$0.21 psf/month (\$2.54 psf)

 - ◉ In Excel, the formula is
=PMT(rate,nper,pv,[fv],[type])
- *Note items [bracketed] in excel formulas do not need to be completed for the formula to calculate.

MODIFIED STRAIGHT-LINE METHOD

EXAMPLE 5

- ◉ Payment (PMT) = \$2.54 psf
- ◉ Compared to Example 1
 - ◉ Contract rent / year: \$20 per square foot
 - ◉ Lease term: 10 years
 - ◉ 10 months free rent, earned one month per year

Calculate Total Rent = \$20 psf x 10 years = \$200.00

Subtract Free Rent = (10 / 12) x \$20 psf = -\$16.67

Equals = Total rent less Free Rent = \$183.33

\$183.33 / 10 years = \$18.33 psf

- ◉ \$18.33 psf - \$2.54 psf = \$15.79 psf

MODIFIED STRAIGHT-LINE METHOD

EXAMPLE 6

- Compared to Example 2 - Straight-Line Method

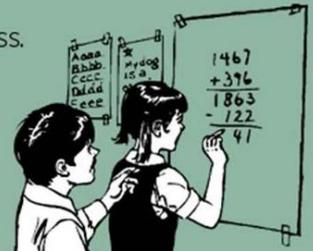
- Contract rent / year: \$14 per square foot
- Lease term: 5 years
- 5 months free rent, earned one month per year
- \$5 per square foot of excess TIs over market
- Calculated the Net Effective Rent at \$11.83 psf

- The landlord borrowed money to provide Tenant Improvement Allowances of \$5 above what the market normally requires. The amount borrowed was amortized at 5.0% interest over a five-year term (the term of the lease).

Billy has 32 pieces of bacon. He eats 28. What does he have now?

Happiness.

Billy has happiness.



MODIFIED STRAIGHT-LINE METHOD

EXAMPLE 6

○ Example

- Contract rent / year: \$14 per square foot
- Lease term: 5 years
- 5 months free rent, earned one month per year

Calculate Total Rent = \$14 psf x 5 years = \$70.00

Subtract Free Rent = (5 / 12) x \$14 psf = -\$5.83

Equals = Total rent less Free Rent = \$64.17

\$64.17 / 5 years = \$12.83 psf

MODIFIED STRAIGHT-LINE METHOD

EXAMPLE 6

- ◉ Calculate the monthly payment for this loan.
- ◉ Present value (PV) = \$5 psf
- ◉ Number of periods (n) = 5 years (60 months)
- ◉ Interest Rate (i) = 5.0%/year (0.42%/month)
- ◉ Future Value (FV) = Nothing

- ◉ Payment (PMT) = \$0.09 psf/month (\$1.13 psf)

- ◉ \$12.83 psf - \$1.13 psf = \$11.70 psf

- ◉ Straight-Line Method vs Modified Straight-Line Method
 - ◉ \$11.83 Vs. \$11.70

LEVEL-EQUIVALENT METHOD

- ◉ Method which fully accounts for the time value of money
- ◉ Calculates the cashflow of the lease and subtracts the landlord's cost of the excess Tenant Improvement Allowance
- ◉ Cons
 - Yield rates aren't as widely published and are more an opinion based on appraiser's judgement

LEVEL-EQUIVALENT METHOD

○ Steps

1. Calculate the annual income for each year
2. Calculate the annual payment for the excess TI loan
3. Subtract the annual payment for the excess TI loan from the annual income
4. Discount the cash flows to a net present value
5. Use the net present value to calculate the annual rent of the uneven cashflows

Excel

=NPV(Rate, Value1, Value2...)

LEVEL-EQUIVALENT METHOD

EXAMPLE 7

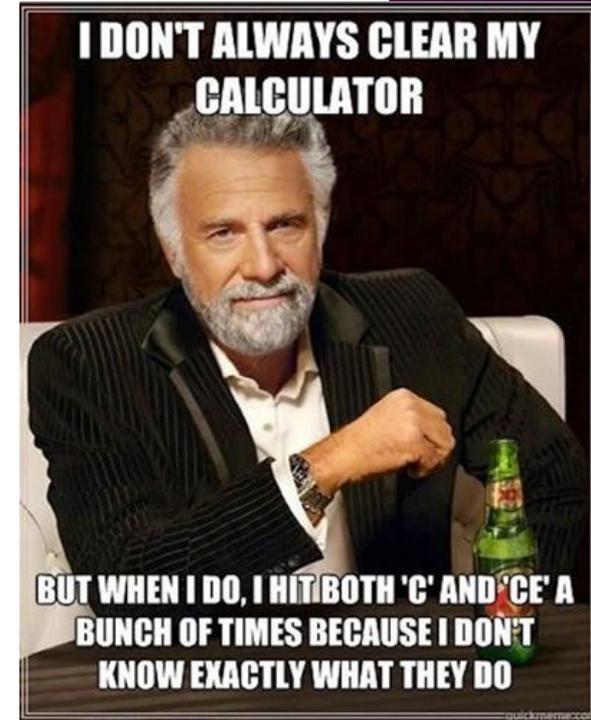
○ Example

- What is the effective rent, using the level-equivalent method, if the appropriate yield rate is 10.0%.
 - Contract Rent is \$20 psf
 - Lease Term is five years
 - Three months free rent, earned one month per year for the first three years
 - Yield rate is 10%
 - No excess tenant improvement allowance

LEVEL-EQUIVALENT METHOD

EXAMPLE 7

- ◉ Need financial calculator or excel, clear calculator
- ◉ Calculate the annual income for each year
- ◉ Year 1 = ($\$20 \text{ psf} \times 11/12 \text{ mos}$) = $\$18.33 \text{ psf}$
- ◉ Year 2 = ($\$20 \text{ psf} \times 11/12 \text{ mos}$) = $\$18.33 \text{ psf}$
- ◉ Year 3 = ($\$20 \text{ psf} \times 11/12 \text{ mos}$) = $\$18.33 \text{ psf}$
- ◉ Year 4 = ($\$20 \text{ psf} \times 12/12 \text{ mos}$) = $\$20.00 \text{ psf}$
- ◉ Year 5 = ($\$20 \text{ psf} \times 12/12 \text{ mos}$) = $\$20.00 \text{ psf}$



LEVEL-EQUIVALENT METHOD EXAMPLE 7



LEVEL-EQUIVALENT METHOD

EXAMPLE 7

- Use the CF_j buttons to enter the annual cashflows into the calculator.
 - 18.33 g CF_j
 - 18.33 g CF_j
 - 18.33 g CF_j
 - 20 g CF_j
 - 20 g CF_j
- Enter the yield rate
 - 10 I
- Solve for NPV
 - f NPV

LEVEL-EQUIVALENT METHOD

EXAMPLE 7

- NPV is \$71.66
 - This is the present value of the unequal cashflows, we still need the annual rates
- To solve for the annual rate, we know the Present Value, Term, yield rate so we can solve for payment.

LEVEL-EQUIVALENT METHOD

EXAMPLE 7

- Present value (PV) = \$71.66 psf
 - Number of periods (n) = 5 years
 - Yield Rate (i) = 10.0%/year
 - Future Value (FV) = Nothing
-
- Payment (PMT) = \$18.90 psf

LEVEL-EQUIVALENT METHOD

EXAMPLE 8

- What is the effective rent, using the level-equivalent method with above-market TI allowances?
 - Contract Rent is \$15 psf
 - Lease Term is four years
 - Three months free rent, earned one month per year for first three years
 - Yield rate is 9.50%
 - Also, the landlord borrowed money to provide Tenant Improvement Allowances of \$10 above what the market normally requires. The amount borrowed was amortized at 5.0% interest over a four-year term (the term of the lease).



LEVEL-EQUIVALENT METHOD

EXAMPLE 8

- ◉ Need financial calculator or excel, clear calculator
- ◉ Calculate the annual income for each year
- ◉ Year 1 = ($\$15 \text{ psf} \times 11/12 \text{ mos}$) = $\$13.75 \text{ psf}$
- ◉ Year 2 = ($\$15 \text{ psf} \times 11/12 \text{ mos}$) = $\$13.75 \text{ psf}$
- ◉ Year 3 = ($\$15 \text{ psf} \times 11/12 \text{ mos}$) = $\$13.75 \text{ psf}$
- ◉ Year 4 = ($\$15 \text{ psf} \times 12/12 \text{ mos}$) = $\$15.00 \text{ psf}$

LEVEL-EQUIVALENT METHOD

EXAMPLE 8

- ◉ Calculate the monthly payment for this loan.
- ◉ Present value (PV) = \$10 psf
- ◉ Number of periods (n) = 4 years (48 months)
- ◉ Interest Rate (i) = 5.0%/year (0.42%/month)
- ◉ Future Value (FV) = Nothing

- ◉ Payment (PMT) = \$0.23 psf/month (\$2.76 psf)

LEVEL-EQUIVALENT METHOD

EXAMPLE 8

- ◉ Calculate the net annual income for each year
- ◉ Year X = Net rent less TI loan payment
- ◉ Year 1 = \$13.75 psf - \$2.76 psf = \$10.99 psf
- ◉ Year 2 = \$13.75 psf - \$2.76 psf = \$10.99 psf
- ◉ Year 3 = \$13.75 psf - \$2.76 psf = \$10.99 psf
- ◉ Year 4 = \$15.00 psf - \$2.76 psf = \$12.24 psf

LEVEL-EQUIVALENT METHOD

EXAMPLE 8

- Use the CF_j buttons to enter the annual cashflows into the calculator.
 - 10.99 g CF_j
 - 10.99 g CF_j
 - 10.99 g CF_j
 - 12.24 g CF_j
- Enter the yield rate
 - 9.50 i
- Solve for NPV
 - f NPV

LEVEL-EQUIVALENT METHOD

EXAMPLE 8

- NPV is \$36.09
 - This is the present value of the unequal cashflows, we still need the annual rates
- To solve for the annual rates, we know the Present Value, Term, yield rate so we can solve for payment.

LEVEL-EQUIVALENT METHOD

EXAMPLE 8

- ◉ Present value (PV) = \$36.09 psf
 - ◉ Number of periods (n) = 4 years
 - ◉ Yield Rate (i) = 9.50%/year
 - ◉ Future Value (FV) = Nothing
-
- ◉ Payment (PMT) = \$11.26 psf

EFFECTIVE RENT AND THE APPROACHES TO VALUE

- Income Approach - Direct Capitalization
 - No adjustment necessary when the subject and comparable sales which were used to derive the cap rates have been extracted have similar rent concessions.
 - Adjustments are necessary when the comparable sales include leases which have been increased by landlord-provided concessions, but the subject is leased at market.

INCOME APPROACH

○ Example

- A 4-tenant office building has some contract rents with concessions that were concluded to be above market. The sale price is \$1,000,000, NOI is \$100,000 and a cap rate of 10.0%. When the Net Effective Rent is used, the NOI decreases to \$90,000. What is the Net Effective Capitalization rate?
- $\$90,000 / \$1,000,000 = 9.0\%$

EFFECTIVE RENT AND THE APPROACHES TO VALUE

○ Sales Comparison Approach

- Development of some adjustments in the sales comparison approach must use effective rent, not contract rent, if rent is used to measure the adjustment.
- Similar to the income approach example, if the sale price is elevated due to excess rent, a deduction of the present value of the excess rent must be made.

SALES COMPARISON APPROACH

○ Example

- The subject property and comparables have different levels of excessive contract rents from landlord-provided concessions.
 - Both differences must be taken into account.
 - Contract rent is 5% greater than the market at the subject property, but the contract rent is 25% greater than the market at the comparable sale. What direction should the adjustment be?
 - A downward adjustment must be made to the comparable sale

SALES COMPARISON APPROACH

◉ Example - Continues

- ◉ Contract rent is 25% greater than the market at the subject property, but the contract rent is 5% greater than the market at the comparable sale. What direction should the adjustment be?
 - An upward adjustment must be made to the comparable sale

SALES COMPARISON APPROACH

○ Example

- Comparable sales have landlord-provided excess concessions in the contract rents. Which way should the sales be adjusted?
 - The sales should be adjusted downward.

EFFECTIVE RENT AND THE APPROACHES TO VALUE

◉ Cost Approach

- If the landlord provided above-standard tenant improvements, those improvements may constitute a form of functional obsolescence due to the excess improvements.

TAX COURT



TAX COURT - MACY'S RETAIL HOLDINGS, INC. V. COUNTY OF HENNEPIN

- ◉ 27-CV-09-15221, 27-CV-10-08453, 27-CV-11-07991, 27-CV-12-10082
- ◉ Filed November 6, 2014
 - Overview - Single, owner-occupied, 89,294 sf free standing furniture showroom facility
 - "Consequently, their differing value conclusions under the income approach turned almost entirely on their different views of market rent."

TAX COURT - MACY'S RETAIL HOLDINGS, INC. V. COUNTY OF HENNEPIN

- Petitioner's appraiser
 - "Where a lease involved tenant improvements or rent concessions, Skare deducted these amounts from base rent and thereby computed for that comparable an *effective* net rent."
- County's appraiser
 - "In contrast to Share, Stoerzinger did *not* reduce base rents by tenant improvements to derive effective net rents."

TAX COURT - MACY'S RETAIL HOLDINGS, INC. V. COUNTY OF HENNEPIN

- ◉ What did the Court say?
 - ◉ Identified two considerations
 - ◉ Magnitude of the tenant improvements
 - ◉ Compatibility of available capitalization rate data

TAX COURT - MACY'S RETAIL HOLDINGS, INC. V. COUNTY OF HENNEPIN

- ◉ Magnitude of the tenant improvements
 - ◉ “Market rent is a measure of income that reflects, among other things, tenant improvement allowances.”
 - ◉ Quotes Supreme court case (EPM I, 797 N.W.2d at 195)
 - ◉ “... Generally, effective market rent is ‘the total of base rent...over the specified lease term minus rent concessions - e.g., free rent [and] *excessive* tenant improvements...”

TAX COURT - MACY'S RETAIL HOLDINGS, INC. V. COUNTY OF HENNEPIN

- "As the foregoing passage makes plain, not all tenant improvements are deducted from base rent when determining effective market rent: a deduction is warranted only where the tenant improvement allowance is 'excessive'."
- "Accordingly, whether tenant improvement allowances should be deducted from market rents to arrive at effective market rents 'must be determined on a case-by-case basis' as a part of the overall determination of market rents."
- "Deductions need be made only for tenant improvements that are 'excessive or atypical'."

TAX COURT - MACY'S RETAIL HOLDINGS, INC. V. COUNTY OF HENNEPIN

- ⦿ Now we know what the Court said, how should they be handled?
 - ⦿ "If tenant improvements are considered as above-the-line expenses, they are subtracted from market rents to determine effective market rents."
 - ⦿ "If, on the other hand, tenant improvements are considered as below-the-line expenses, they are addressed through the selection of the appropriate capitalization rate."

TAX COURT - MACY'S RETAIL HOLDINGS, INC. V. COUNTY OF HENNEPIN

- Capitalization rate selection
 - A net operating income *reduced by tenant improvements* that is capitalized using a rate derived from a net operating income *not reduced by tenant improvements* results in an artificially lowered value indication.
 - Consistency is key.

TAX COURT - MACY'S RETAIL HOLDINGS, INC. V. COUNTY OF HENNEPIN

- Capitalization rate selection - Example
 - Hypothetical sale - \$14 contract rent, 5 year term, 5 months free rent, \$5 excess TI and \$1,400,000 sale price

Income Approach - Actual Income			
Office Revenue	Net Rent	Square Feet	Annual Income
Potential Gross Income	\$14.00	10,000	\$140,000
Vacancy and Collection Loss	5%		\$7,000
Effective Gross Income			\$133,000
Total Office Revenue			\$133,000
Office Operating Expenses	Per Square Foot	Square Feet	Annual Expenses
Unreimbursed Operating Expenses	\$9.00	500	\$4,500
Replacement Allowance	\$0.30	10,000	\$3,000
Total Office Expenses			\$7,500
Net Operating Income (NOI)			\$125,500
Capitalization Rate			
Overall Rate			8.75%
Effective Tax Rate			0.19%
			8.94%
Sale Price			\$1,400,000

TAX COURT - MACY'S RETAIL HOLDINGS, INC. V. COUNTY OF HENNEPIN

- Capitalization rate selection - Example
 - Effective net rent is \$11.83 psf and the sale price is still \$1,400,000.

Income Approach - Actual Income			
Office Revenue	Net Rent	Square Feet	Annual Income
Potential Gross Income	\$11.83	10,000	\$118,300
Vacancy and Collection Loss	5%		\$5,915
Effective Gross Income			\$112,385
	Total Office Revenue		\$112,385
Office Operating Expenses	Per Square Foot	Square Feet	Annual Expenses
Unreimbursed Operating Expenses	\$9.00	500	\$4,500
Replacement Allowance	\$0.30	10,000	\$3,000
	Total Office Expenses		\$7,500
Net Operating Income (NOI)			\$104,885
Capitalization Rate			
Overall Rate			?
Effective Tax Rate			0.19%
			?
Sale Price			\$1,400,000

Loaded Cap Rate is 7.49%

Overall Rate is 7.30%.

TAX COURT - MACY'S RETAIL HOLDINGS, INC. V. COUNTY OF HENNEPIN

- ◉ 27-CV-07-07774, 27-CV-08-13026, 27-CV-09-15232
- ◉ Filed November 28, 2011
 - Overview - Two-story, 128,271 sf, anchor department store
 - "We agree with Mr. Skare that the J.C. Penney's interior remodeling costs should not be considered in determining rent in this case."

TAX COURT - MACY'S RETAIL HOLDINGS, INC. V. COUNTY OF HENNEPIN

⦿ Rental Comparable 1

- ⦿ J.C. Penney leased the property "as is" and then projected spending \$4 million on interior remodeling to convert to a J.C. Penney.
- ⦿ "Mr. Skare did not consider the \$4 million interior remodeling because it does not change the rent paid."

TAX COURT - NORTHWESTERN NATIONAL LIFE INSURANCE COMPANY V. COUNTY OF HENNEPIN

- ◎ TC-18794
- ◎ Filed June 21, 1995
 - Overview - Mid-rise, office-data center in Downtown Minneapolis
 - Using Net Effective Rent in a DCF

TAX COURT - NORTHWESTERN NATIONAL LIFE INSURANCE COMPANY V. COUNTY OF HENNEPIN

○ Petitioner's Appraiser

- "First, Mr. Jabs used effective net rent in his DCF so that the expenses of tenant improvements and leasing costs were deducted before he entered any data in his DCF."

○ County's Appraiser

- "Mr. Boris used net rent and deducted the cost of tenant improvement and leasing costs as DCF expenses."

TAX COURT - NORTHWESTERN NATIONAL LIFE INSURANCE COMPANY V. COUNTY OF HENNEPIN

⦿ What did the Court say?

- ⦿ “We used Mr. Boris’ net rent model, however, because it allows us to “see” each expense of the Property in the DCF.”

TAX COURT - LOAN OAK ROGERS, L.L.C. V. COUNTY OF HENNEPIN

- ◉ 27-CV-11-06077, 27-CV-12-05686, 27-CV-13-07180
- ◉ Filed April 9, 2015
 - Overview - Bulk warehouse facility and adjoining unimproved parcel
 - Appraiser failed to take into account lease concessions.

TAX COURT - LOAN OAK ROGERS, L.L.C. V. COUNTY OF HENNEPIN

- Court quotes The Appraisal of Real Estate
 - “Concessions are provided by landlords when demand is weak and there is increased competition among landlords to attract new tenants. It is not unusual for free rent concessions to be given outside of the lease term so that the concessions do not appear on the written lease contract. In these situations appraisers must still consider the lease concessions when calculating the effective net rent being paid. Concessions together with tenant installation allowances influence market rent estimates.”

DISCUSSION

- What have you seen from Petitioners?

THANK YOU AND
ENJOY THE NICE WEATHER



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