Appraisal Methodology for Economic Development Bond Leaseholds in Georgia

CAVEAT Program presentation May 19, 2015 by James D. Vernor MAI, PhD

I. Background, Introduction and Structuring the deal

II. The early, long form model

A. Benefits to leasehold include

1. **Any savings in occupancy costs due to rent obligations of tenant being less than the going market rents at the time**

2. **The value at the end of the program of the property**

B. Appraisal data to be gathered by appraisal staff includes many inputs

Values are developed for each January first of the bond term using DCF and, probably, a large spreadsheet. (One early spreadsheet was 24 columns by 78 rows)

III. The revised short form model

1. **With shorter term bond deals, the principal and interest payments wipe out any bargain in comparison to market rents, so**

2. **There is no "income" advantage, and**

3. **The entire benefit to the leasehold is in the reversion.**

4. **Data requirements are vastly reduced;**

5. **If reversion is stated as a nominal $1 the PV calculations generate the "ramp-up" schedule. (See exhibit)**

IV. Evolution of doing the Math -- a short history

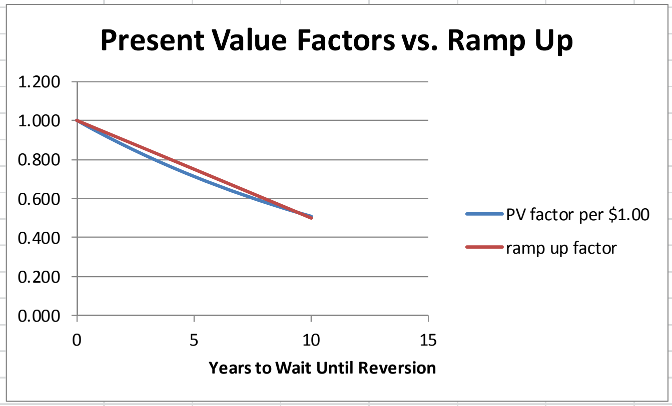
A. Time Value of Money algebra

B. Tables of Six Functions based on the algebra

C. Financial calculators such as the Hewlett Packard 12C

D. Computer spreadsheet applications such as Excel

DEMONSTRATION OF A RAMP-UP SCHEDULE			
FOR ECONOMIC DEVELOPMENT BONDS			
			J D Vernor 12/30/2013
Using the formula $PV = FV/ (1 + i)^n$			
Executed by the Excel PV function			
Input judgements:			
Term (years)	10		
Discount rate (%)	0.07		
Years to wait until reversion	PV factor per $1.00	ramp up factor	
10	0.508	0.50	
9	0.544	0.55	
8	0.582	0.60	
7	0.623	0.65	
6	0.666	0.70	
5	0.713	0.75	
4	0.763	0.80	
3	0.816	0.85	
2	0.873	0.90	
1	0.935	0.95	
0	1.000	1.00	



VI 3 important cases/laws

<u>Harris DeKalb, 1981</u>

Trial court found that a leasehold interest was taxable (BOA said it was fee simple—or, later, a usufruct under Allright Parking) and BOE developed a formula for its valuation: subtract value of LF from Value of FS to get VLH; GA superior court affirmed. Theory is out of favor by 2000. Decision goes on to define a five year–plus agreement as an estate for years.

<u>OCGA 36-80-16.1(e)</u> enacted 2009 indicates assessors may use simplified valuation methods for leaseholds that are not arbitrary or unreasonable and that no one method is prescribed. A 50% starting point must be demonstrated and not assumed.

<u>Macon Bibb County Board of Tax Assessor et al v. Atlantic Southeast Airlines D</u>efined “usufruct”

VII Issues and challenges

A. If an appraiser were to do the long form model, and if real estate taxes to the leasehold are to be omitted, should the effective tax rate be added to the TVM discount rate? Is the effective tax rate indicated by the “Ramp-up rate”?

B. The long form model gave prospective leaseholders many bargaining points, drawing out the process and impacting result.

C. Taxpayer opposition groups will argue at the bond validation hearing that the ramp-up schedule is arbitrary and the whole structure should be rejected; “Phantom Bonds”