



MAAO

Minnesota Association
of Assessing Officers

Multi-Topics for Multi-Family

—

An Apartment Symposium



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CIA Valuations Committee

- **Klein & Blonigen**
Multi-Topics for Multi-Family
- **Brad Moore**
**Assisted Living Facilities:
Allocation of Real Estate Value**
- **Question & Answer**

CIA Valuations Committee



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Multi-Topics for Multi-Family

By Tim Klein & Dan Blonigen

Overview



- Apartment Market Update
- The Income Approach
- Outstate Appraisal
- Mass Appraisal Techniques

- Question & Answers throughout

Apartment Market Update



- Premier Asset Class since 2011
- Low Vacancy = Rent Growth
- Historically low cost of debt & equity
- Record sales volume
- Rising values!

Twin Cities Average Rent



- 4Q 2016 – Y-O-Y Rent growth of 4.0%

- 1 Bedrooms Average Rent
 - ▣ Downtown Minneapolis - \$1,423
 - ▣ Maple Grove/Osseo/Rogers - \$1,131
 - ▣ Woodbury - \$1,037
 - ▣ Minnetonka - \$1,025
 - ▣ Bloomington - \$923
 - ▣ Shakopee - \$851

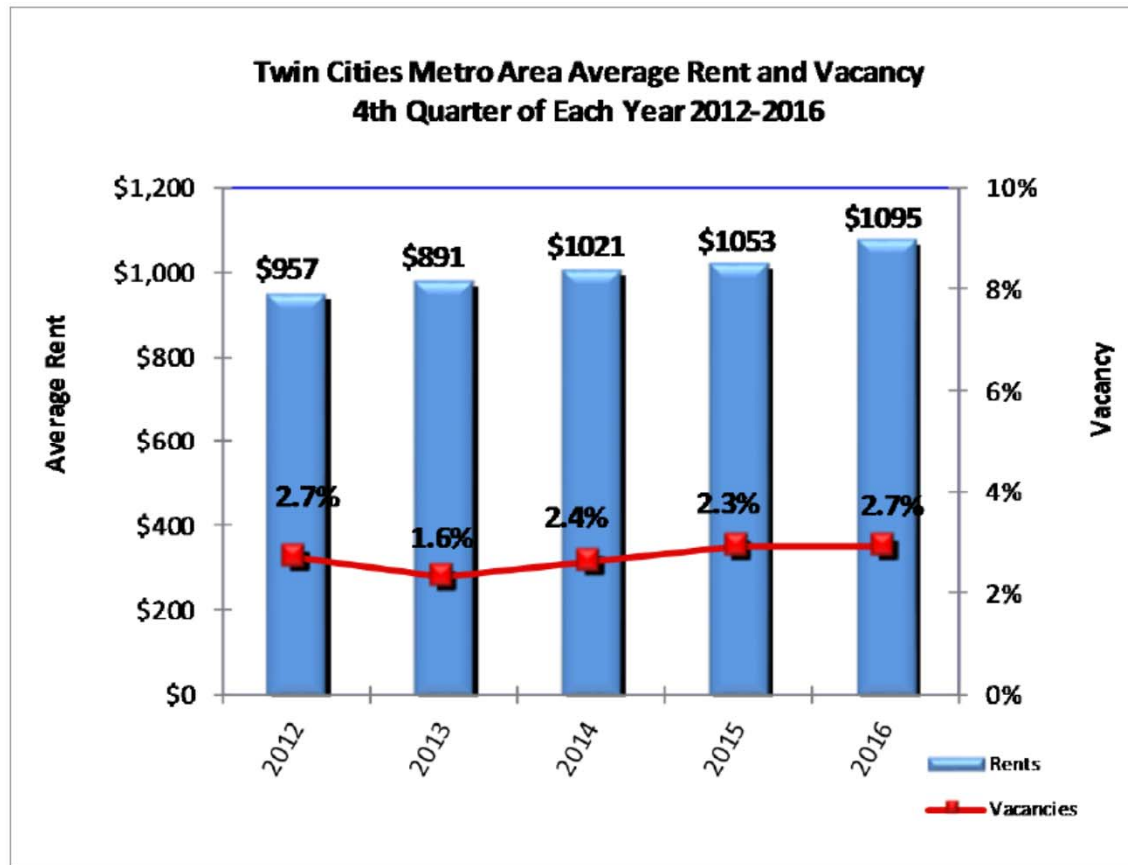
*Source: GVA Marquette Advisors 4Q2016

Twin Cities Average Rent

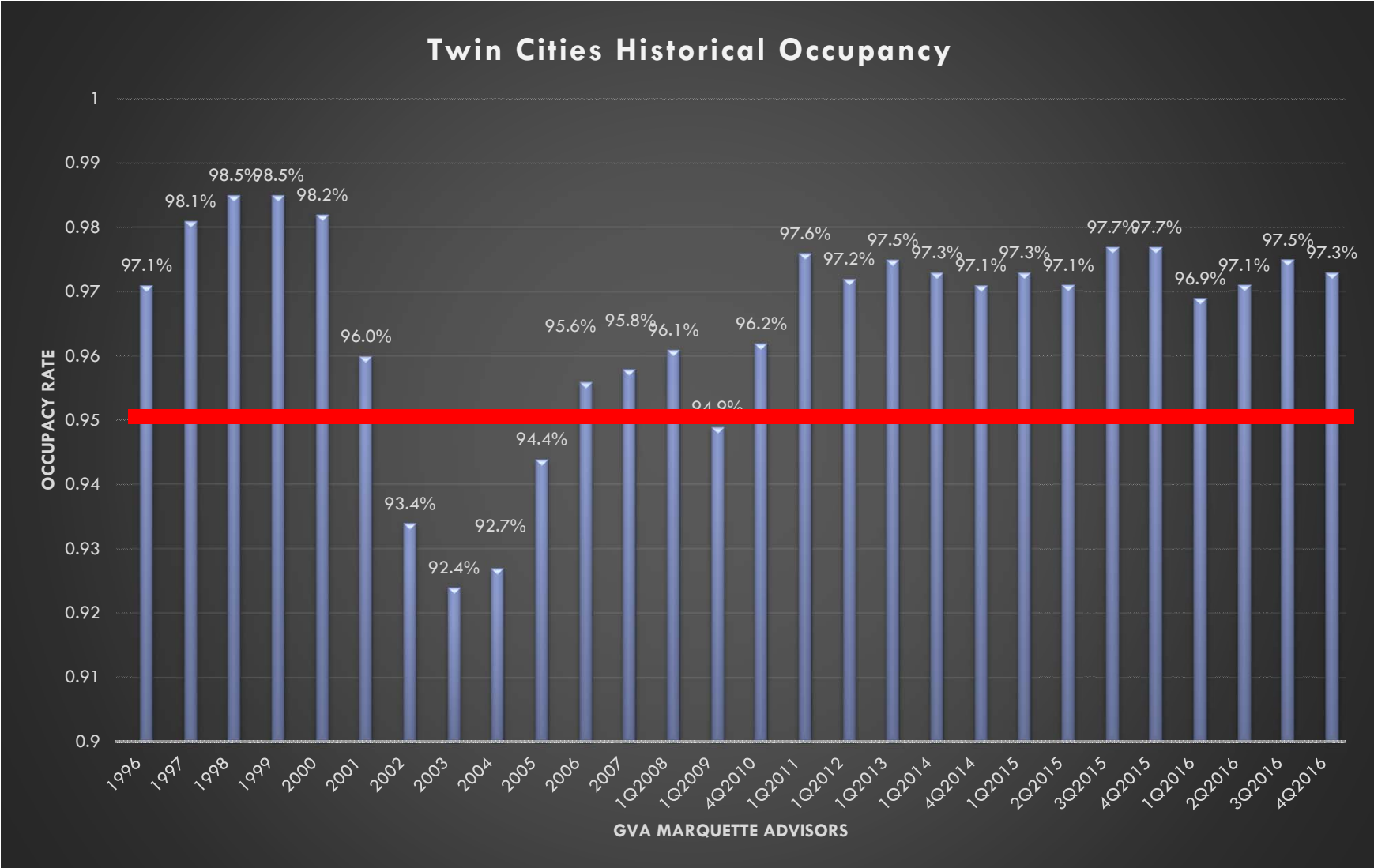


Twin Cities Vacancy Rates

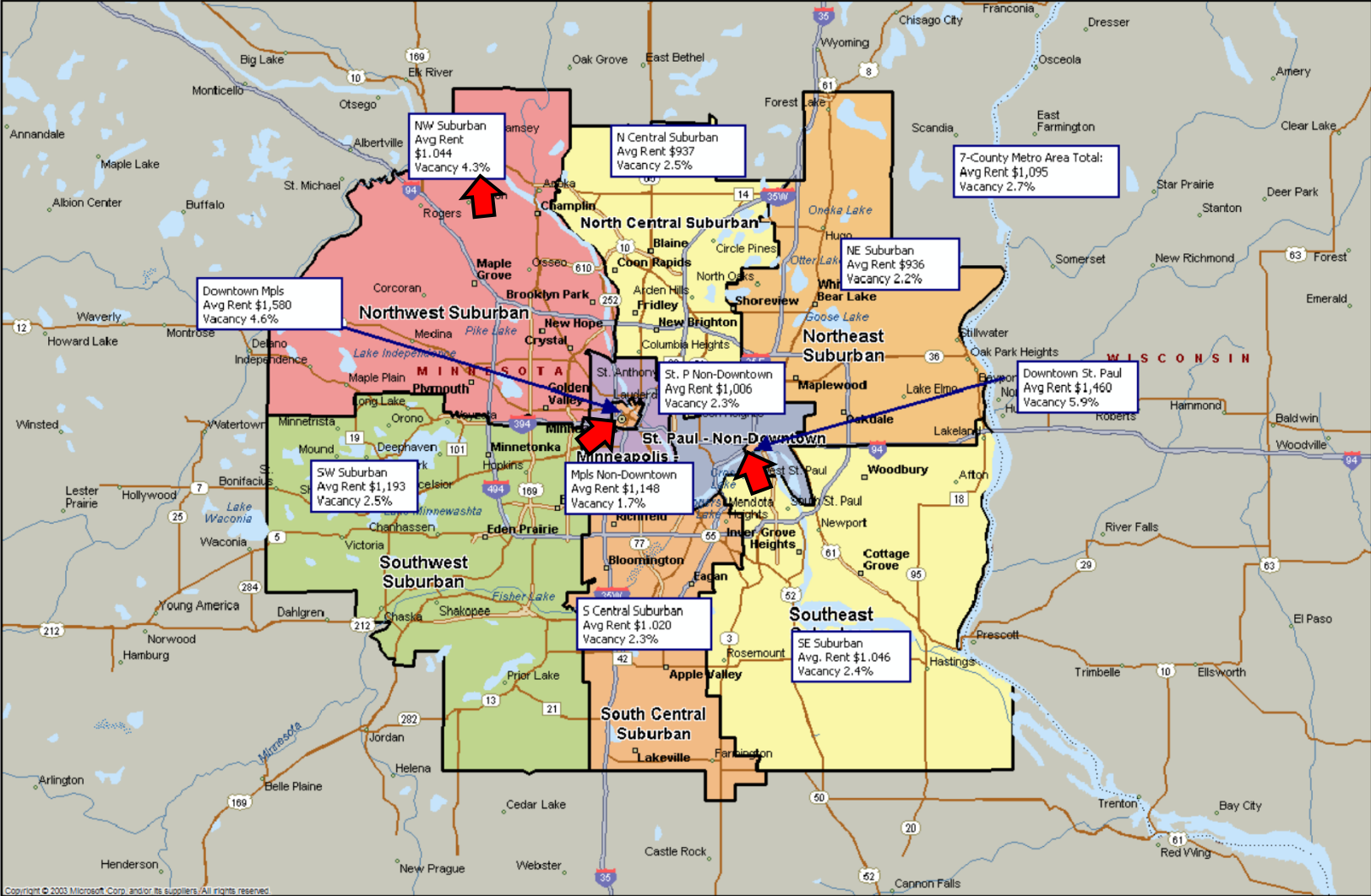
- Overall vacancy of 2.7%



Twin Cities Occupancy Rates

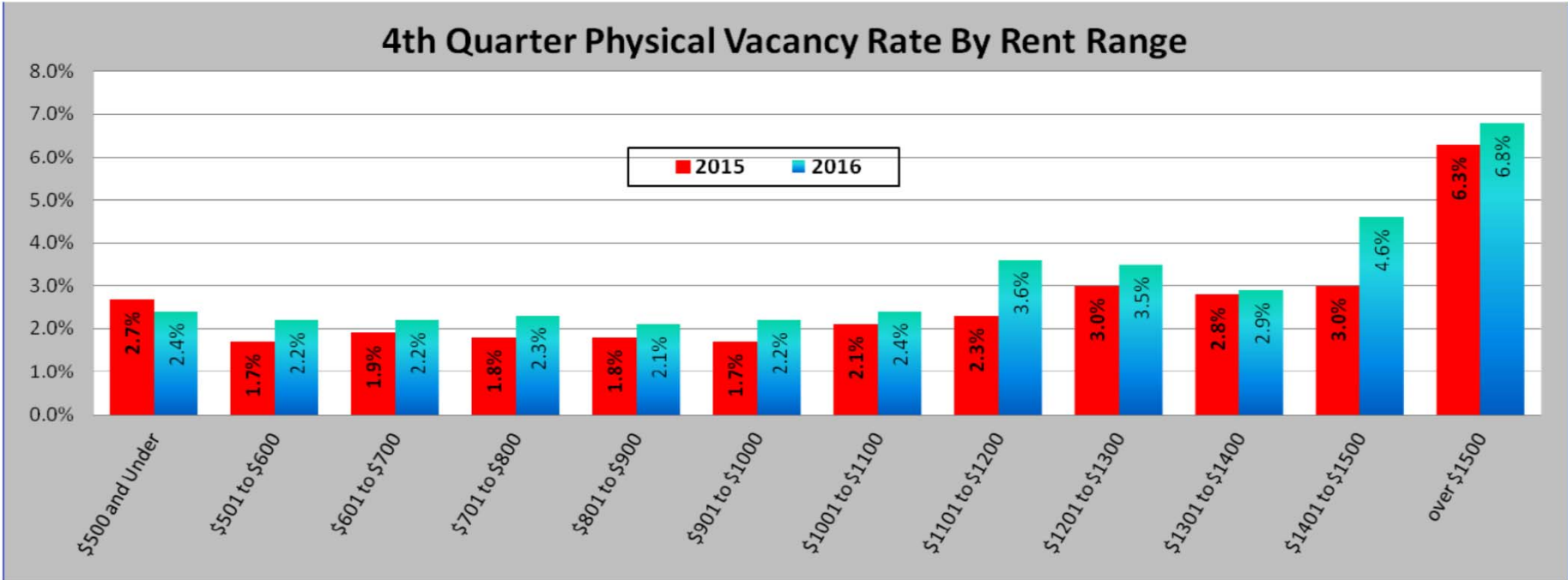


Twin Cities Market Trends 4Q 2016



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TC Vacancy by Rent Range



2017 National Multifamily Index

- Minneapolis-St. Paul – 4th highest ranked metro by Marcus Millichap.

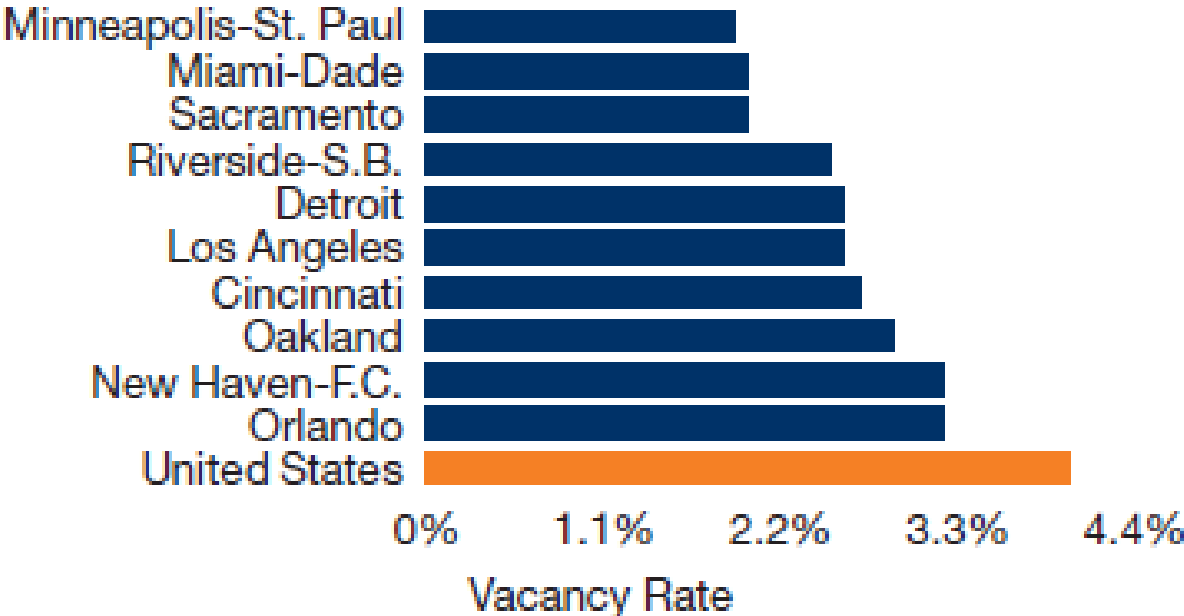
Market Name	Rank 2017	Rank 2016 ¹	16-17 Change
Los Angeles	1	11	↗ 10
Seattle-Tacoma	2	9	↗ 7
Boston	3	10	↗ 7
Minneapolis-St. Paul	4	7	↗ 3
Oakland	5	4	↘ -1
Portland	6	8	↗ 2
San Francisco	7	1	↘ -6
San Jose	8	2	↘ -6
San Diego	9	5	↘ -4
New York City	10	3	↘ -7



Expected 2017 Vacancy

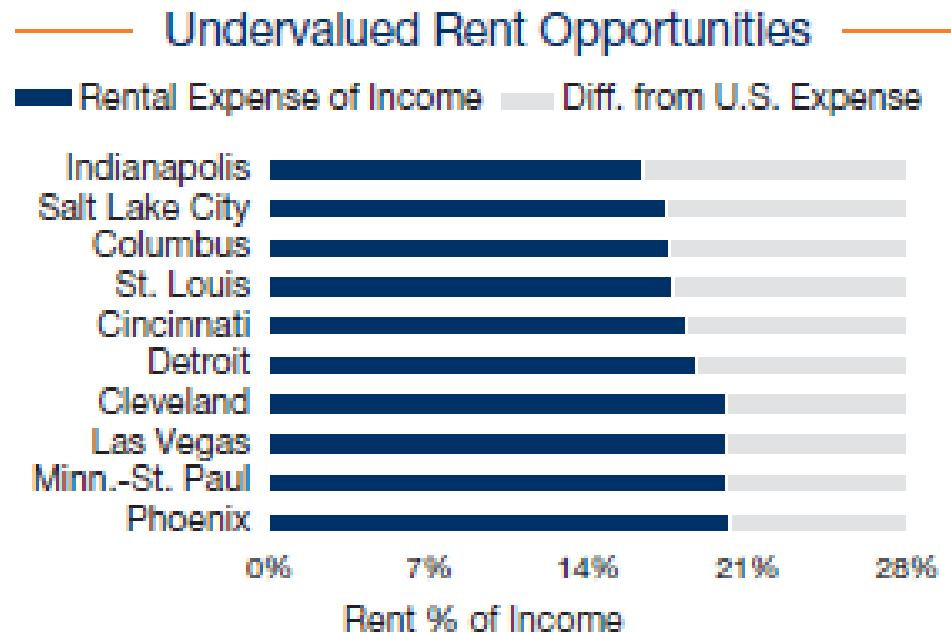


Markets with the Lowest Expected 2017 Vacancy Rates



Affordability Index

- MSP Median Income 20% higher than national average
- MSP monthly rent is below national average.



Where is demand coming from?

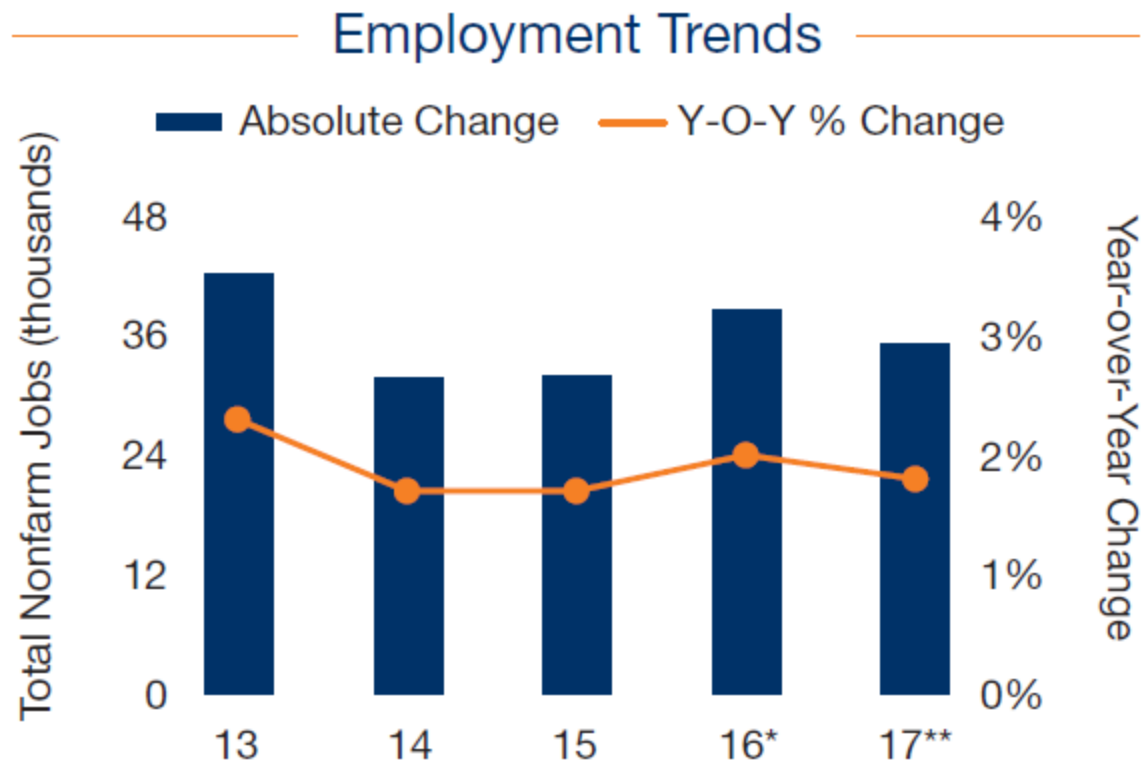
- Job Growth

- Demographics
 - Prime rental age 20-34
 - Largest Generation - Millennials (Age 19-35)
 - Renters by choice
 - Baby Boomers?

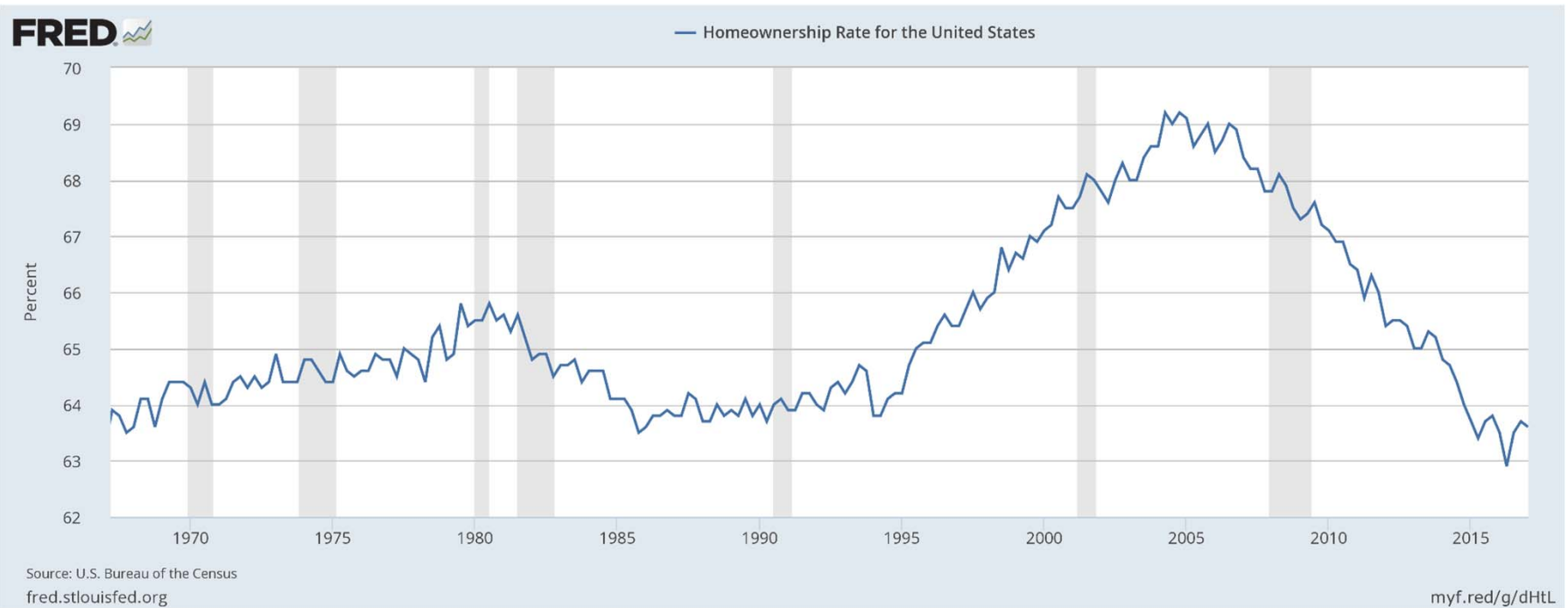
- Lack of housing

Employment Trends

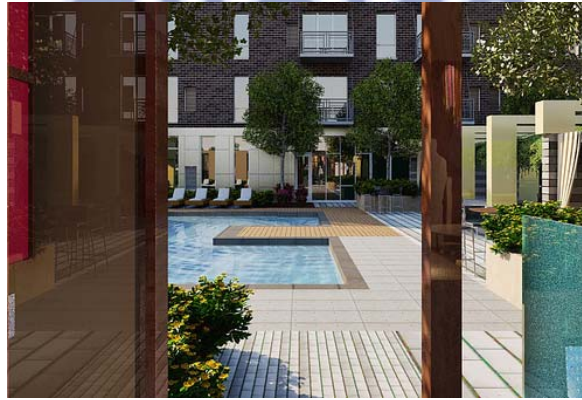
- Twin Cities expected to add 35,000 jobs in 2017.



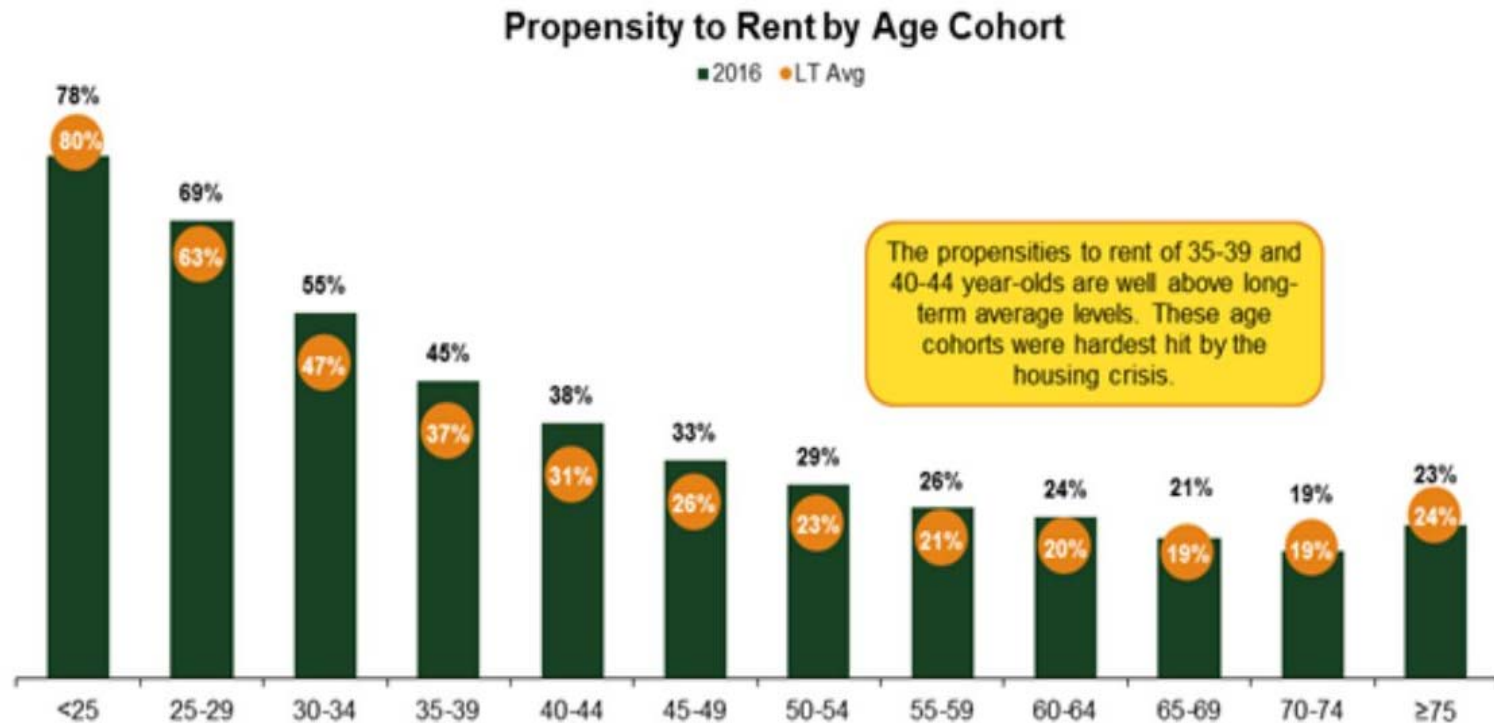
Renter Nation



Renters by Choice



Propensity to Rent by Age Cohort

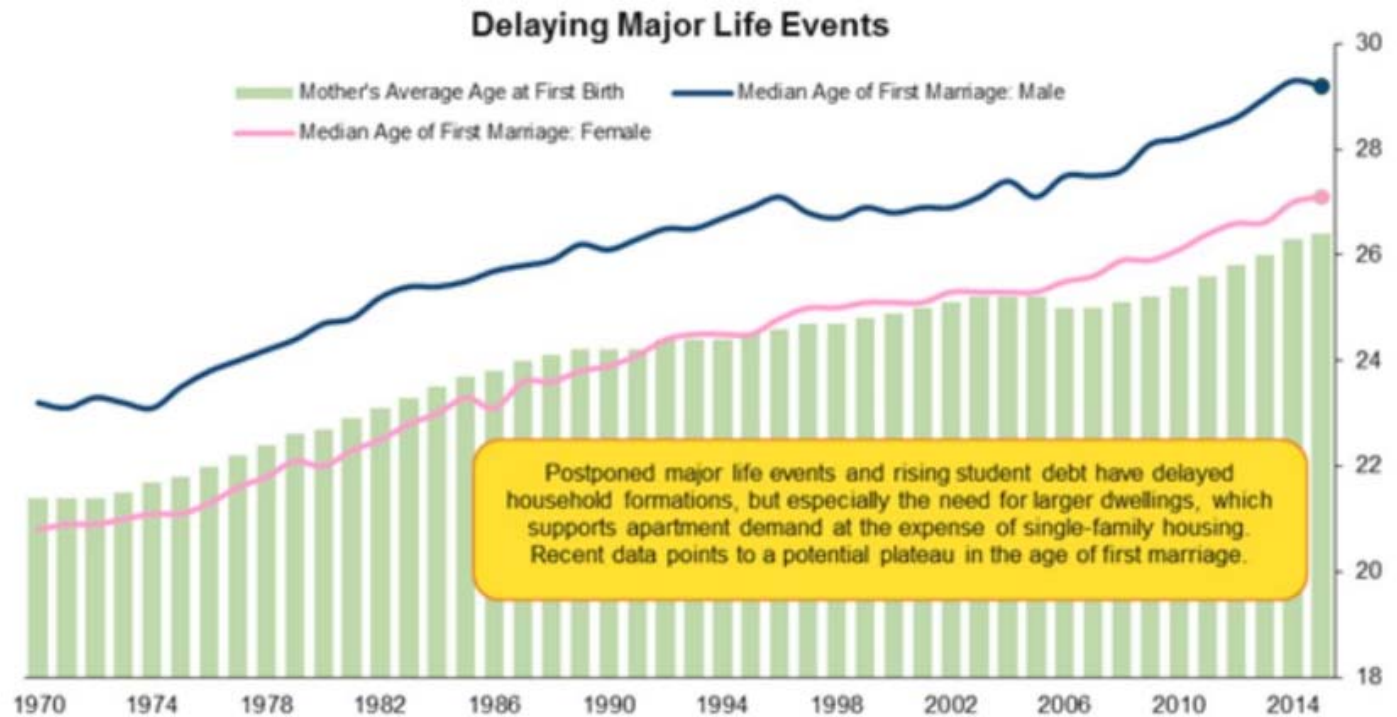


Millennials

They Are 2015's Largest Generation

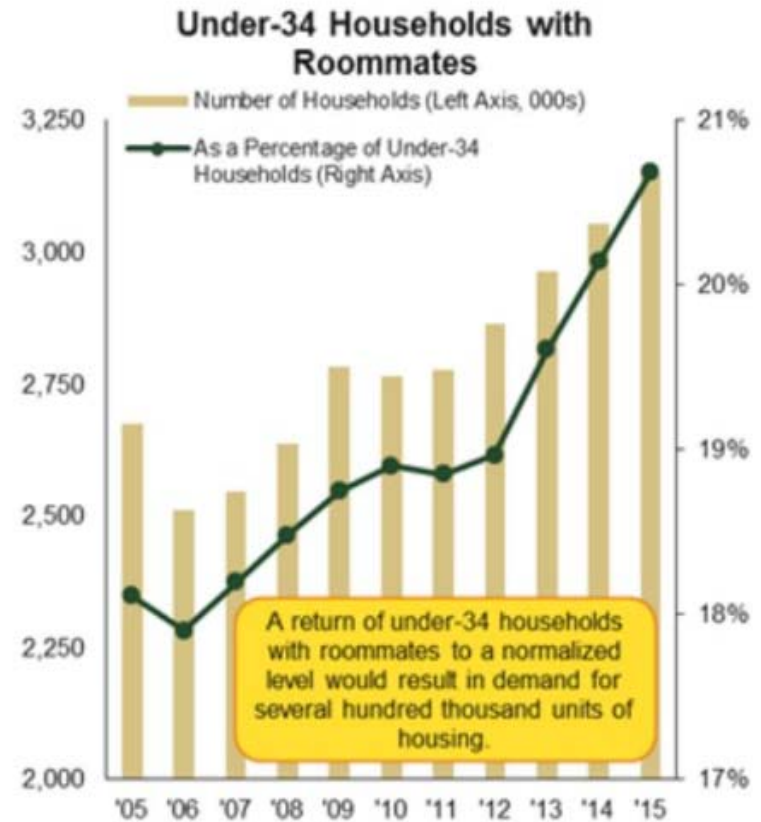
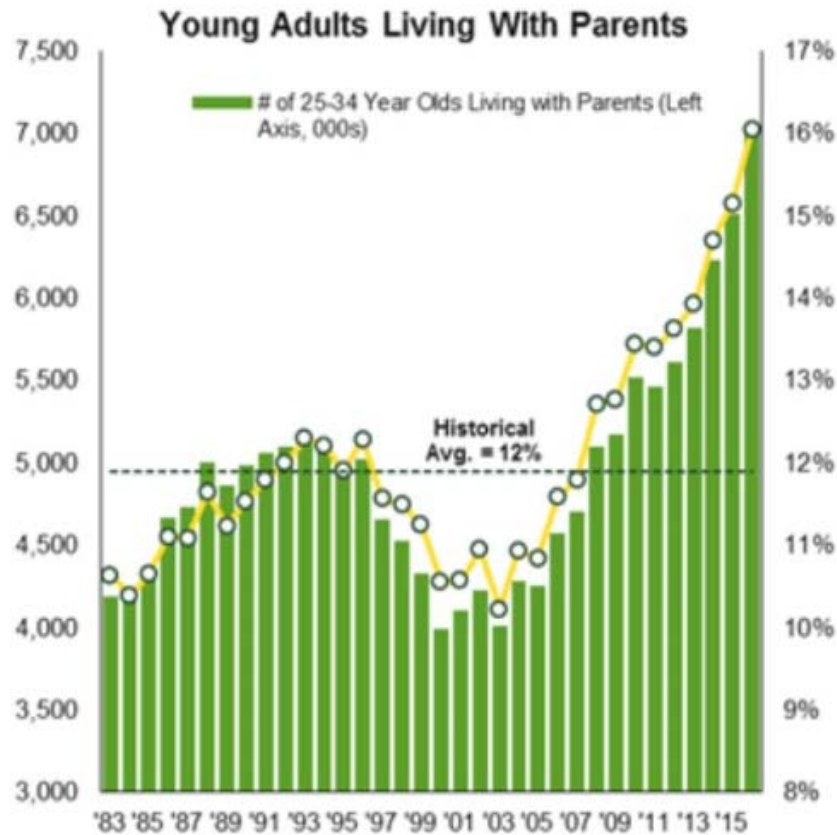


Delayed Life Events



Source: U.S. Census Bureau, CDC

Significant Pent-Up Demand

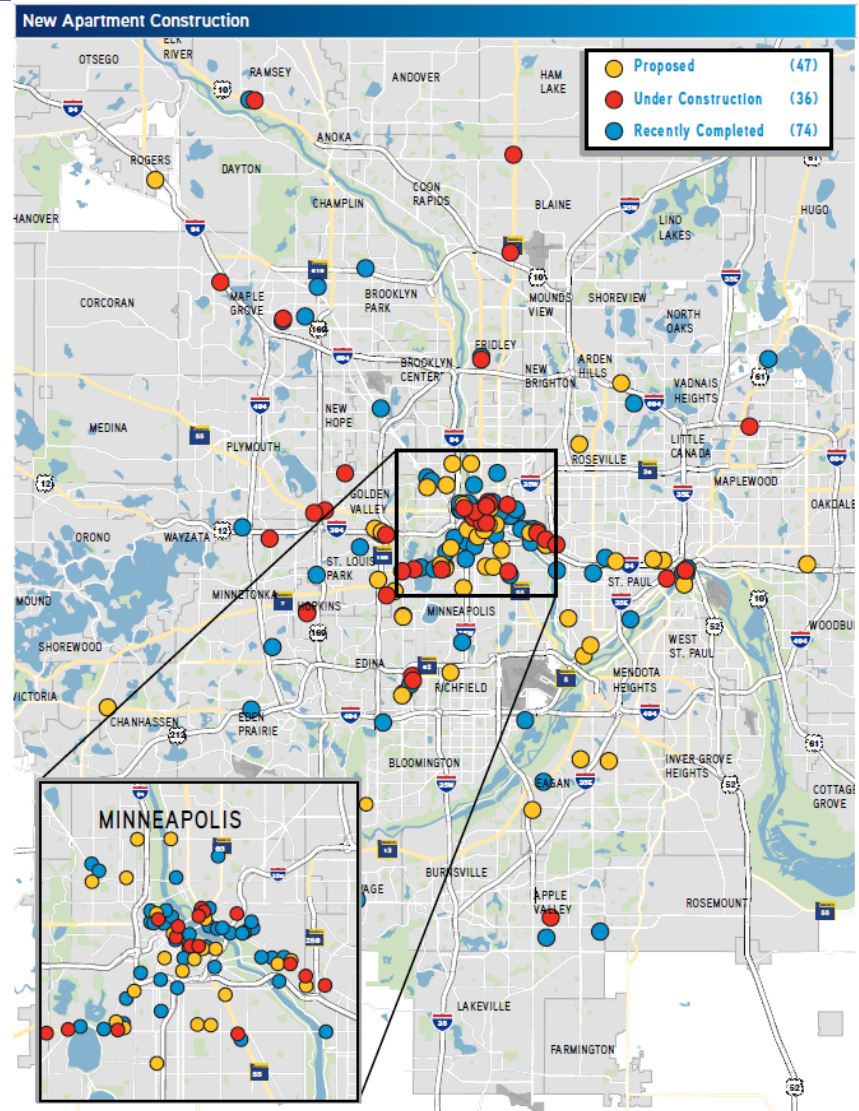


Source: Bureau of Labor Statistics and U.S. Census Bureau.

New Supply

- 2016 -3,290 new units
- 2017 – 5,000 new units

- In comparison, Denver
 - 2016 -10,700
 - 2017 -11,900



Sales



- 2016 – Record \$1.5 Billion in sales volume.
- 2017 – Expected to be over \$1 Billion.
- B & C Properties in most demand
- Emphasis on value add

Cap Rates – 2017 Assessment

- Class A – 5.0-5.5%
- Class B – 5.5-6.0%
- Class C – 6.0-6.5%



Sales: Sartell vs Bloomington

Heritage Village, Sartell, MN

- \$102,900 per Unit
- Avg rent: \$966
- 5.9% cap rate
- GIM 8.9



Covington, Bloomington, MN

- \$194,200 per Unit
- Avg rent: \$1,577
- 5.4% cap rate
- GIM 10.3

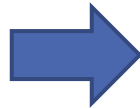


Trends Recap

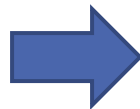
□ Market Rent



□ Vacancy



□ Cap Rates



The Income Approach

The Income Approach

- An appraiser analyzes a property's capacity to generate future income benefits and capitalizes the income into an indication of value.
- The principle of anticipation is fundamental...

Direct Capitalization - Overview

- Process of converting a single year's income into an indication of value
- NOI (Net Operating Income)
- **Divided by**
- Capitalization Rate
- =VALUE

Direct Capitalization - Overview

- Process of converting a single year's income into an indication of value
- PGI (Potential Gross Income)
- - **Vacancy**
- EGI (Effective Gross Income)
- - **Expenses**
- NOI (Net Operating Income)
- **Divided by**
- Capitalization Rate
- =VALUE

Direct Capitalization - Overview

8 – Unit Apt



Calculate NOI

- \$70,000 (PGI)
- -5,000(Vac)
- \$65,000 (EGI)
- -\$32,000 (Expenses)
- NOI = \$33,000

Direct Capitalization - Overview

8 – Unit Apt



Direct Cap

- NOI = \$33,000
- **Divided by**
- Cap = 8.25%

- Calculate the value
 - ▣ \$400,000

Direct Capitalization Approach

General procedure to valuing property via the direct capitalization approach

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- Step 6: Capitalize Net Operating Income

Hypothetical Property Analysis

- Non-existing property-Used for Demonstration Purposes
- Minnesota Apartment-Built in 1986
- 50 Units
- Average amenity package
- 30 Detached Garage Stalls
- 10 Storage Lockers

Potential Gross Apartment Income

- Projecting Potential Gross Apartment Income
 - ▣ Historical and current subject rent (Rent Roll)
 - Has rent been increasing/decreasing
 - Is occupancy too high? Potential for rent increase?
 - ▣ Survey rent comparables
 - ▣ Rent adjustment analysis
 - Location, unit size, in unit amenities (washer/dryer), complex amenities, parking, parking fee, age/condition, utilities included in rent, etc.
 - ▣ Market studies
 - GVA Marquette Advisors-Quarterly Apartment Trends
 - ▣ Supply/Demand
 - Current demand
 - Proposed projects?

Rent Roll

Unit	Resident Name	Rent
310	Brettingen	\$ 995.00
	4/30/2013	
	1 garage	
311	Soholt, Alf & June	\$ 995.00
	5/31/2013	
	1 garage	
312	Anderson, Harlan/Theresa	\$ 995.00
	10/31/2013	
313	Leino, Samuel & Carol	\$ 995.00
	9/30/2013	
314	Bell, Ralph Jr. / Blair, Scott	\$ 1,000.00
	5/31/2013	
315	Gross / Johnson	\$ 995.00
	11/30/2013	

Rent Comparables

- Units of Comparison
 - ▣ Rent per unit
 - ▣ Rent per square foot (per month)
 - ▣ Rent per room (student housing)

- Adjust for:
 - ▣ Included Amenities
 - ▣ Included Utilities
 - ▣ Concessions

Apartment Rent Comparables

Comparable #	SUBJECT	#1	#2	#3
Address	123 1st Street N	125 1st Street N	1000 Oak Drive	450 Main Street
City	New Hope	New Hope	New Hope	New Hope
Year Built	1961	1971	1969	1971
# Units	68	70	44	79
Occupancy	98%	100%	92%	95%
Data Month/Year	Jan-13	Jan-13	Jan-13	Jan-13
AMENITIES				
By Unit	Range/oven, Refrig., D/W, Disposal, Wall A/C	Range/oven, Refrig., D/W, Wall A/C	Range/oven, Refrig., D/W, Disposal, Wall A/C	Range/oven, Refrig., D/W, Disposal, Wall A/C
By Complex	Community room, fitness center, storage, elevator	Community room, fitness center, storage, elevator	Outdoor pool, Community room, storage, elevator	Community room, fitness center, storage, elevator
UNIT TYPES				
1 Bedroom				
# 1BRs	12	32	10	30
Size	700	700	675	700
Rent	\$ 750	\$ 725	\$ 750	\$ 750
Rent PSF	\$ 1.07	\$ 1.04	\$ 1.11	\$ 1.07
2 Bedroom				
# 2BRs	44	32	24	30
Size	850	900	800	825
Rent	\$ 900	\$ 925	\$ 900	\$ 900
Rent PSF	\$ 1.06	\$ 1.03	\$ 1.13	\$ 1.09
3 Bedroom				
# 3BRs	12	6	10	19
Size	1,000	975	1,000	1,100
Rent	\$ 1,000	\$ 975	\$ 1,025	\$ 1,050
Rent PSF	\$ 1.00	\$ 1.00	\$ 1.03	\$ 0.95
CONCESSIONS				
	None	None	\$300 off 1st month	None

Potential Gross Apartment Income

□ Subject Projection

POTENTIAL GROSS APARTMENT INCOME						
Unit Type	# of Units		Projected Monthly Rent		# of Months	Projected Annual Rent
1-BR/1-BA Unit (700 Square Feet)	30	x	\$750	x	12	= \$270,000
2-BR/2-BA Unit (850 Square Feet)	20	x	\$900	x	12	= \$216,000
Projected Gross Apartment Income	50	x	\$810	x	12	= \$486,000

Potential Gross Parking/Garage Income

□ Projecting Potential Gross Parking Income

- Survey comparable properties
- Typical parking rent
 - Included in rent or additional fee?
 - Detached/Attached/Tuck Under/Underground/Surface?
 - Downtown/Uptown/Dinkytown Mpls/St. Louis Park-\$100-\$150 per month
 - Twin Cities suburban area-\$45 to \$100 per month
 - Outside the Twin Cities metropolitan area-\$25 to \$50 per month

POTENTIAL GROSS PARKING/GARAGE INCOME

	<u># of Stalls</u>		<u>Rent Per Month</u>		<u># of Months</u>		
Potential Gross Garage Income	30	x	\$50	x	12	=	\$18,000

Income Capitalization Approach

General procedure to valuing property via the direct capitalization approach

- Step 1: Determine market rents
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Apartment Vacancy/Credit Loss Analysis

- Subject historical vacancy and credit loss
- Survey comparables in the market
- Market studies
 - ▣ GVA Marquette Advisors
- Is vacancy a bad thing?
- Typical credit loss?

Rent Concessions/Loss to Lease



- Look at comparables
- Market studies
- Interview real estate professionals/property managers
- Revenue management systems (Yieldstar)

Parking Vacancy/Credit Loss Analysis

- Subject's historical vacancy/credit loss
- Parking vacancy comparables
- Interview property managers
- Parking ratio analysis
- Type of property/location
 - ▣ Senior housing/Affordable Housing versus Market Rate
 - ▣ Light Rail-Bus Lines

Market Vacancy

Comparable #	SUBJECT	#1	#2	#3
Address	123 1st Street N	125 1st Street N	1000 Oak Drive	450 Main Street
City	New Hope	New Hope	New Hope	New Hope
Year Built	1961	1971	1969	1971
# Units	68	70	44	79
Occupancy	98%	100%	92%	95%
Data Month/Year	Jan-13	Jan-13	Jan-13	Jan-13

- Occupied 252
- Total Units 261
- Vacancy indicated by subject and rent comparables: 3.4%

Market Vacancy

Twin Cities Metro Area									
Unit Type	Units Surveyed	Units Vacant	Avg Rent 3/2013	Avg Rent 3/2012	% Change	Vacancy 3/2013	Vacancy 3/2012	Change	
Studio	5,320	147	\$727	\$687	5.7%	2.8%	2.6%	0.1%	
One Bedroom	49,307	1,208	\$843	\$812	3.7%	2.4%	2.7%	-0.2%	
One + Den	2,291	68	\$1,159	\$1,121	3.4%	3.0%	2.6%	0.3%	
Two Bedroom	48,092	1,426	\$1,048	\$1,015	3.2%	3.0%	2.9%	0.1%	
Two + Den	1,071	46	\$1,474	\$1,445	2.0%	4.3%	3.5%	0.8%	
Three Bedroom	5,990	184	\$1,332	\$1,294	2.9%	3.1%	3.4%	-0.3%	
Three Den/Four	312	12	\$1,692	\$1,633	3.6%	3.8%	6.6%	-2.7%	
Total	112,383	3,091	\$966	\$935	3.3%	2.8%	2.8%	-0.1%	
New Hope									
Unit Type	Units Surveyed	Units Vacant	Avg Rent 3/2013	Avg Rent 3/2012	% Change	Vacancy 3/2013	Vacancy 3/2012	Change	
Studio	12	0	\$632	\$630	0.2%	0.0%	8.3%	-8.3%	
One Bedroom	710	6	\$740	\$705	5.0%	0.8%	2.5%	-1.7%	
Two Bedroom	686	5	\$870	\$836	4.1%	0.7%	2.9%	-2.2%	
Three Bedroom	65	1	\$1,123	\$1,093	2.7%	1.5%	1.5%	0.0%	
Total	1,491	12	\$817	\$783	4.3%	0.8%	2.7%	-1.9%	

- The projected vacancy of 3.4% appears to be reasonable and supported by market data.

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Effective Gross Ancillary Income

- Miscellaneous Income
 - Laundry, month to month fees, application fees, early termination fees, vending, security deposit forfeits, recovered collection loss, pet revenue, guest unit, late fees, move out charges, NSF (non-sufficient funds) charges, phone/internet/cable commissions.
- RUBS (ratio utility billing system) Income
 - Utilities (typically water/sewer/trash) are not individually metered and tenant is charged back their pro-rata share of utilities.
- Storage Locker Income
 - Included or additional charge
 - \$5 to \$25 per month

Example Other Income

Subject's Segmented Other Income		
	Year End 2014	\$/Unit
Garage Income	\$60,532.61	\$113
Storage Income	\$30,733.86	\$58
Pet Fee	\$60,472.40	\$113
Other Income		
Late Fee	\$38,597.80	\$72
Transfer Fee	\$2,000.00	\$4
Forfeited Deposits	\$16,781.20	\$31
NSF Fee	\$2,640.00	\$5
Early Termination Fees	\$64,331.32	\$120
Eviction & Legal Fees	\$4,660.00	\$9
Admin/Cleaning Fee	\$39,175.00	\$73
Application Fee	\$20,585.00	\$39
Vending Income	\$1,048.00	\$2
Misc Income	\$48,427.98	\$91
Video/Marketing Commissions	\$24,533.76	\$46
Interest Income	\$3,034.62	\$6
Less: Deposit	-\$1,320.21	-\$2
Laundry Income	\$119,307.06	\$223
SUBTOTAL	\$383,801.53	\$719
Rubs Income		
Trash Fee	\$30,506.17	\$57
Gas Income	\$209,758.46	\$393
Water Income	\$116,868.62	\$219
Utility Processing Fee	\$20,244.11	\$38
Pest Control	\$6,101.25	\$11
	\$377,377.36	\$718
TOTAL	\$912,918	\$1,710

Effective Gross Income

- Potential Gross Income (PGI)
 - ▣ Deduct market vacancy
 - ▣ Deduct credit loss
 - ▣ Add Other Income
- Effective Gross Income (EGI) - the anticipated income from all operations of the real property adjusted for vacancy and collection losses.

Effective Gross Income

□ Subject Projection

EFFECTIVE GROSS INCOME CALCULATION						
<u>INCOME PROJECTIONS:</u>						
Unit Type	<u># of Units</u>		<u>Projected Monthly Rent</u>		<u># of Months</u>	<u>Projected Annual Rent</u>
1-BR/1-BA Unit (700 Square Feet)	30	x	\$750	x	12	\$270,000
2-BR/2-BA Unit (850 Square Feet)	20	x	\$900	x	12	\$216,000
Projected Gross Apartment Income	50	x	\$810	x	12	\$486,000
Less: Vacancy and Credit Loss Allowance @ 5.00%						(\$24,300)
Effective Gross Apartment Income						\$461,700
Potential Gross Garage Income	<u># of Stalls</u>		<u>Rent Per Month</u>		<u># of Months</u>	
	30	x	\$50	x	12	\$18,000
Less: Vacancy and Credit Loss Allowance @ 5.00%						(\$900)
Effective Gross Garage Income						\$17,100
Effective Gross Miscellaneous Income (50 Units x \$150 Per Unit)						\$7,500
Effective Gross RUBS Income						\$0
Effective Gross Storage Locker Income (10 Units x \$10 Per Month x 12 Months x 90% Occupancy)						\$1,080
Rent Concessions/Loss to Lease:						\$0
TOTAL EFFECTIVE GROSS INCOME -- ALL SOURCES						\$487,380

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Operating Expense Projections

- Standardized Expense Categories
 - ▣ Real Estate Tax
 - ▣ Insurance
 - ▣ Utilities
 - Gas
 - Electricity
 - Water/Sewer/Trash
 - ▣ Repairs and Maintenance
 - ▣ Management (% of Effective Gross Income)
 - ▣ Advertising
 - ▣ Administration
 - ▣ Caretaker/Payroll
 - ▣ Reserves for Replacement

Operating Expense Projections

- Subject's historical operating expenses
 - ▣ Trends in expenses-% annual increases
- Expense comparables
 - ▣ Trends in comparables
 - ▣ Are comparable expense categories grouped similar to the subject

Owners Income Expense

Owner's Information (from CPA)	
Management (including manager's 1-bedroom apartment)	\$5,000
Insurance (3 years premiums)	\$31,461
Real estate taxes	\$10,206
Maintenance	\$6,991
Common utilities	
Electric	\$2,097
Gas	\$1,049
CATV	\$0
Water & sewer	\$1,398
Debt service	\$62,563
Automobile expense	\$1,600
Depreciation	\$19,701
Miscellaneous (incl. admin/tel/office)	\$2,097
Owner's salary(owner does maintenance)	\$25,000
Total	\$169,163



Non-Allowable Expenses



- Depreciation
- Capital Improvements
- Owner's Personal Expenses
- Debt Service

Expenses – Real Estate Taxes

- Allowable Expense but...
- Can be handled two ways
 - ▣ As a line item expense
 - ▣ Loading the cap rate with Effective Tax Rate
- MN Tax Court dictates a Loaded Cap

Replacement Allowance

- An allowance that provides for the periodic replacement of building components that wear out more rapidly than the building itself and must be replaced during the building's economic life; sometimes referred to as *reserves*
- *Example: Roof is replaced every 20 yrs at a cost of \$40,000.*

Operating Expense Projections

□ Subject Projection

OPERATING EXPENSE PROJECTION			
EXPENSE PROJECTIONS:	% of EGI	Per Unit	Annually
Real Estate Tax	12.82%	\$1,250	\$62,500
Insurance	2.05%	\$200	\$10,000
Utilities	8.21%	\$800	\$40,000
Repairs and Maintenance	10.26%	\$1,000	\$50,000
Management (3.50% of EGI)	4.00%	\$390	\$19,500
Advertising	1.03%	\$100	\$5,000
Administration	1.54%	\$150	\$7,500
Caretaker/Payroll	8.21%	\$800	\$40,000
Reserves for Replacement	2.56%	\$250	\$12,500
Total Operating Expenses Including Reserves	50.68%	\$4,940	\$247,000

NET OPERATING INCOME

- Net Operating Income (NOI): the actual or anticipated income remaining after all operating expenses are deducted from effective gross income, but before mortgage debt service and book depreciation are deducted. May be calculated before or after deducting replacement reserves.

NET OPERATING INCOME

- Subject Projection

NET OPERATING INCOME PROJECTION	
Total Effective Gross Income--All Sources	\$487,380
Less: Total Operating Expenses Inc. Reserves	(\$247,000)
NET OPERATING INCOME	\$240,380
Per Unit:	\$4,808

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CAPITALIZATION RATE ANALYSIS

- ▣ Market Extraction Method-Use of Comparable Sales
 - Trailing capitalization rate
 - How is trailing calculated?
 - Pro-forma capitalization rate
 - Value added deal
- ▣ Band of Investment Method
- ▣ Surveys
 - Korpacz
 - RERC
- ▣ Broker Discussions
 - CBRE
 - NAI Everest
 - Moran and Company
- ▣ Risk?

CAPITALIZATION RATE ANALYSIS



CAPITALIZATION RATE EXAMPLE					
Sale Price \$3,210,000					
	Trailing 12 Month	Trailing 9 Month Annualized	Trailing 6 Month Annualized	T1 Inc. Annualized/ T12 Expenses	Year 1 Pro-Forma
Net Operating Income	\$210,576 6.56%	\$219,885 6.85%	\$225,342 7.02%	\$233,688 7.28%	\$240,750 7.50%

Cap Rates

□ RERC Real Estate Report

MINNEAPOLIS

2ND QUARTER 2012

Minneapolis Investment Criteria First-Tier ¹ Investment Properties													
	Pre-Tax Yield (%)			Going-In Cap Rate (%)			Terminal Cap Rate (%)			Anticipated 1-Year Growth Rates			
	RERC Estimate	Midwest Region	U.S.	RERC Estimate	Midwest Region	U.S.	RERC Estimate	Midwest Region	U.S.	National Value	Midwest Value	National Rent	Midwest Rent
Offc - CBD	8.9	9.4	9.2	7.3	7.8	7.5	8.0	8.5	8.2	1.7	1.2	1.6	0.9
Offc - Suburban	9.5	9.8	9.6	7.8	8.3	8.0	8.4	8.8	8.6	1.0	0.3	0.8	0.1
Ind - Warehouse	9.1	9.4	9.4	7.6	8.1	7.9	8.2	8.7	8.5	1.7	1.7	1.5	1.5
Ind - R&D	9.4	9.7	9.7	8.0	8.4	8.2	8.5	8.9	8.7	1.2	0.9	1.0	0.6
Ind - Flex	9.6	9.8	9.7	8.1	8.5	8.2	8.7	9.0	8.8	1.1	0.9	1.0	0.6
Ret - Reg Mall	8.9	9.1	9.1	7.2	7.5	7.6	8.0	8.3	8.3	1.0	0.9	0.8	0.6
Ret - Pwr Center	9.1	9.2	9.3	7.6	7.8	7.7	8.2	8.5	8.5	0.9	0.8	0.7	0.5
Ret - Neigh/ Comm.	9.1	9.3	9.4	7.7	8.1	7.8	8.3	8.7	8.6	1.3	1.0	1.1	0.6
Apartment	7.8	8.2	8.3	6.3	6.9	6.5	6.9	7.5	7.1	3.9	3.7	3.6	3.8
Hotel	10.3	10.4	10.4	8.7	8.8	8.6	9.1	9.4	9.2	2.1	2.0	2.1	1.8
Average	9.2	9.4	9.4	7.6	8.0	7.8	8.2	8.6	8.5	1.6	1.3	1.4	1.1

¹ First-tier investment properties are defined as new or newer quality construction in prime to good locations.
Source: RERC Investment Survey.

Cap Rates

□ PwC Real Estate Investor Survey (Korpacz)

Table 28 NATIONAL APARTMENT MARKET Second Quarter 2013					
	CURRENT	LAST QUARTER	1 YEAR AGO	3 YEARS AGO	5 YEARS AGO
DISCOUNT RATE (IRR)^a					
Range	5.00% – 14.00%	5.00% – 14.00%	5.25% – 14.00%	6.25% – 14.00%	6.00% – 10.50%
Average	8.04%	8.06%	8.30%	9.89%	8.16%
Change (Basis Points)		- 2	- 26	- 185	- 12
OVERALL CAP RATE (OAR)^a					
Range	3.50% – 10.00%	3.50% – 10.00%	3.75% – 10.00%	5.00% – 11.00%	3.50% – 8.00%
Average	5.70%	5.73%	5.76%	7.68%	5.75%
Change (Basis Points)		- 3	- 6	- 198	- 5
RESIDUAL CAP RATE					
Range	4.25% – 9.75%	4.25% – 9.75%	4.50% – 9.75%	5.50% – 11.00%	4.50% – 8.50%
Average	6.18%	6.22%	6.15%	7.84%	6.69%
Change (Basis Points)		- 4	+ 3	- 166	- 51
MARKET RENT CHANGE^b					
Range	(2.00%) – 7.00%	(2.00%) – 6.00%	(2.00%) – 8.00%	(10.00%) – 3.00%	0.00% – 8.00%
Average	2.60%	2.57%	2.80%	(0.49%)	3.17%
Change (Basis Points)		+ 3	- 20	+ 309	- 57
EXPENSE CHANGE^b					
Range	1.00% – 3.50%	1.00% – 3.50%	1.00% – 4.00%	0.00% – 4.00%	2.00% – 3.75%
Average	2.67%	2.71%	2.65%	2.38%	2.92%
Change (Basis Points)		- 4	+ 2	+ 29	- 25
MARKETING TIME^c					
Range	0 – 18	0 – 18	0 – 18	1 – 18	1 – 12
Average	5.1	5.1	5.3	7.1	6.0
Change (▼, ▲, =)		=	▼	▼	▼

a. Rate on unleveraged, all-cash transactions

b. Initial rate of change

c. In months

Income Capitalization Approach

General procedure to valuing property via the direct capitalization approach

- Step 1: Determine market rents
- Step 2: Determine and apply market vacancy and credit loss
- Step 3: Determine any additional ancillary income
- Step 4: Project stabilized operating expenses
- Step 5: Project market capitalization rate
- Step 6: Capitalize Net Operating Income

Direct Capitalization Value

□ Subject Projection

DIRECT CAPITALIZATION	
Net Operating Income	\$240,380
Capitalization Rate	<u>7.50%</u>
FEE SIMPLE MARKET VALUE INDICATION	\$3,205,067
ROUNDED TO:	\$3,210,000
Per Unit	\$64,200

Value Add Properties

CAPITALIZATION RATE ANALYSIS

- Value added deals
 - ▣ 1980's vintage apartments
 - ▣ Upgrades to appliances, countertops, cabinets, bathrooms, flooring, etc.
 - ▣ Results in aggressive capitalization rate due to upside potential

CAPITALIZATION RATE ANALYSIS

□ Value Added Property Example-Hypothetical

PROPERTY	<u>#1</u>	<u>#2</u>	<u>#3</u>	<u>#4</u>	<u>#5</u>
Cost to Upgrade Per Unit	\$750	\$1,500	\$2,500	\$3,500	\$5,000
Monthly Rent Premium	\$25	\$50	\$75	\$100	\$150
Multiplied by 12 Months:	<u>12</u>	<u>12</u>	<u>12</u>	<u>12</u>	<u>12</u>
Annual Rent Premium	\$300	\$600	\$900	\$1,200	\$1,800
Multiplied by Proj. Occupancy	95%	95%	95%	95%	95%
Multiplied by Proj. Expense Ratio (45%)	<u>55%</u>	<u>55%</u>	<u>55%</u>	<u>55%</u>	<u>55%</u>
Annual Net Operating Income Premium	\$157	\$314	\$470	\$627	\$941
Divided by Projected Capitalization Rate	<u>6.50%</u>	<u>6.50%</u>	<u>6.50%</u>	<u>6.50%</u>	<u>6.50%</u>
Upgraded Value Per Unit	\$2,412	\$4,823	\$7,235	\$9,646	\$14,469
Less: Cost to Upgrade	<u>\$750</u>	<u>\$1,500</u>	<u>\$2,500</u>	<u>\$3,500</u>	<u>\$5,000</u>
Additional Net Value Created-Per Unit	\$1,662	\$3,323	\$4,735	\$6,146	\$9,469

Outstate Appraisal

Outstate Appraisal Analysis



- Challenges to outstate appraisal
 - ▣ Limited data
 - ▣ Affordable housing supply
 - ▣ Larger geographic area to analyze

Outstate Appraisal Analysis



- Determining Market Rent
 - Rent rolls
 - Look at market rate and affordable properties
 - Interview property managers
 - Looking at properties from a larger geographic area

Outstate Appraisal Analysis

- Other/Miscellaneous Income
 - Application fees, late charges, month to month premiums, forfeited security deposits, chargebacks, and pet rent.
 - Garage Rent
 - Apartments (Underground/Detached): \$25 to \$75 per month
 - Townhouses (Attached): Typically included in rent
 - RUBS

Outstate Appraisal Analysis

- Vacancy Rate and Collection Loss
 - ▣ Historical information
 - ▣ Talk with property managers
 - ▣ Market studies
 - ▣ Market rate vs. affordable housing

Outstate Appraisal Analysis

□ Expense Projections

■ Look at historical statements for properties

- Do the statements include real estate taxes, insurance, utilities, repairs and maintenance, management, advertising, administration, and payroll?
- Does the market support all expense categories?

<u>Operating Expenses</u>	<u>Annually</u>	<u>Per Unit</u>	<u>% EGI</u>
Real Estate Tax	\$41,000	\$1,108	11.71%
Insurance	\$8,687	\$235	2.48%
Utilities	\$34,641	\$936	9.89%
Repairs and Maintenance	\$17,662	\$477	5.04%
Management Fee	\$0	\$0	0.00%
Advertising	\$0	\$0	0.00%
Administration	\$0	\$0	0.00%
Caretaker/Payroll	\$0	\$0	0.00%
Total Operating Expenses	\$101,990	\$2,756	29.13%

Outstate Appraisal Analysis

□ Comparables

- Look at expense comparables from the market or similar markets
- What is included in repairs/payroll?

<u>Operating Expenses</u>	<u>Annually</u>	<u>Per Unit</u>	<u>% EGI</u>
Real Estate Tax	\$117,500	\$1,175	11.49%
Insurance	\$21,350	\$214	2.09%
Utilities	\$77,213	\$772	7.55%
Repairs and Maintenance	\$243,561	\$2,436	23.81%
Management Fee	\$51,150	\$512	5.00%
Advertising	\$7,231	\$72	0.71%
Administration	\$15,421	\$154	1.51%
Caretaker/Payroll	\$165,245	\$1,652	16.15%
Total Operating Expenses	\$698,671	\$18,883	68.30%

Outstate Appraisal Analysis

- Capitalization Rates

- Analyze listings

- Look at all outstate comps available

- Costar

- Broker Interviews

- Loopnet

- Look at the spread between metro and outstate

Minneapolis	Bemidji	Rochester	Staples
5.00%	6.39%	6.00%	7.96%

Outstate Appraisal Analysis

□ Capitalization Rates

▣ Market surveys

Regional Investment Criteria - 4Q 2016 Third-Tier ¹ Investment Properties											
	Office		Industrial			Retail			Apartment	Student Housing	Hotel
	CBD	Suburban	Warehouse	R&D	Flex	Regional Mall	Power Center	Neigh/Comm			
West Investment Criteria											
Pre-tax Yield (IRR) (%)											
Range	7.3 - 12.0	7.5 - 12.0	6.5 - 11.0	7.8 - 12.0	7.8 - 11.5	7.5 - 12.0	7.8 - 12.0	7.0 - 11.0	7.0 - 12.0	7.5 - 11.0	9.0 - 13.5
Average	9.5	9.6	8.9	9.6	9.5	9.3	9.5	9.3	8.7	9.3	11.1
Going-In Cap Rate (%)											
Range	5.8 - 9.0	6.0 - 9.3	5.5 - 9.5	5.5 - 9.5	5.5 - 9.5	6.0 - 9.0	6.0 - 9.0	5.0 - 9.0	4.5 - 8.8	5.5 - 8.5	7.0 - 11.0
Average	7.3	7.6	7.2	7.5	7.5	7.3	7.7	7.3	6.2	6.8	8.7
Terminal Cap Rate (%)											
Range	6.0 - 11.0	6.5 - 11.0	6.5 - 9.8	7.0 - 10.0	6.5 - 10.0	6.0 - 10.0	6.0 - 10.0	7.0 - 9.5	5.5 - 9.0	6.0 - 9.5	7.0 - 11.5
Average	8.2	8.5	8.0	8.3	8.3	8.0	8.3	7.9	7.0	7.4	9.3
Midwest Investment Criteria											
Pre-tax Yield (IRR) (%)											
Range	9.0 - 13.0	9.0 - 12.0	9.0 - 13.0	6.5 - 11.5	9.0 - 13.0	6.0 - 11.0	6.0 - 11.0	6.0 - 11.3	7.3 - 12.0	8.8 - 11.3	10.0 - 13.0
Average	10.5	10.6	10.3	10.3	10.7	9.5	10.0	10.1	9.6	9.6	11.1
Going-In Cap Rate (%)											
Range	7.0 - 10.1	6.8 - 10.2	6.5 - 10.1	7.0 - 12.1	7.0 - 10.5	7.3 - 12.0	6.5 - 10.3	7.0 - 12.1	6.0 - 11.0	6.8 - 9.0	7.0 - 12.1
Average	8.8	8.8	8.7	9.3	9.2	9.3	8.9	9.1	8.1	7.9	9.8

Mass Appraisal

Mass Appraisal

- Separate by Class
- Isolate the variables.
 - ▣ PGI
 - ▣ Vacancy
 - ▣ Operating Expenses
 - ▣ Cap Rate
- Extract Trends
 - ▣ Or
- Create a Model

Mass Appraisal - Trends



CLASS C											
2013		2014									
<u>BASE PRO FORMA</u>		<u>RENT CHANGE</u>		<u>VACANCY CHANGE</u>		<u>CAP RATE CHANGE</u>		<u>TAX RATE CHANGE</u>		<u>Total PRO FORMA</u>	
Rent	1	Rent	1.03	Rent	1	Rent	1	Rent	1	Rent	1.03
Vac	0.05	Vac	0.05	Vac	0.03	Vac	0.05	Vac	0.05	Vac	0.03
NOI	0.95	NOI	0.9785	NOI	0.97	NOI	0.95	NOI	0.95	NOI	0.9991
Cap	8.50%	Cap	8.50%	Cap	8.50%	Cap	8.00%	Cap	8.50%	Cap	0.08
Tax	1.85%	Tax	1.85%	Tax	1.85%	Tax	1.85%	Tax	1.95%	Tax	0.0195
Loaded	10.35%	Loaded	10.35%	Loaded	10.35%	Loaded	9.85%	Loaded	10.45%	Loaded	0.0995
Value	9.178744	Value	9.4541063	Value	9.3719807	Value	9.64467	Value	9.0909091	Value	10.041206
		Change	3.00%	Change	2.11%	Change	5.08%	Change	-0.96%		9.40%

Mass Appraisal Model

INCOME PRO FORMA - 2014 ASSESSMENT								
SAMPLE MASS APPRAISAL								
OLD CEDAR AVE S								
BLOOMINGTON, MN								
# of UNITS	Model Name	Unit Type	Estimated SF per Unit	Estimated Total SF	Economic Market Rent per Month	Economic Market Rent per SF	Monthly Economic Market Rent	
2		Efficiency	400	800	\$515	\$1.29	\$1,030	
73		1 Bedroom	875	63,875	\$715	\$0.82	\$52,195	
27		2 Bedrooms	1,150	31,050	\$945	\$0.82	\$25,515	
3		3 Bedrooms	1,650	4,950	\$1,300	\$0.79	\$3,900	
105	Total Units			100,675	NRA	\$0.82	\$82,640	
50	Garages				\$30		\$1,500	
	Monthly Market Rent						\$84,140	
	Annual Market Rent						\$1,009,680	
CAPITALIZATION PROCESS								
POTENTIAL GROSS INCOME (PGI)								\$1,009,680
LESS: VACANCY & COLLECTION LOSS								
% OF PGI								5.00%
								(\$50,484)
OTHER INCOME:								1.00% of PGI
								\$10,097
EFFECTIVE GROSS INCOME (EGI)								\$969,293
LESS: ANNUAL OPERATING EXPENSES								
% OF EGI								35.00%
								\$3,231
LESS: ANNUAL RESERVES FOR REPLACEMENT								\$250/unit
								2.71%
TOTAL ANNUAL ALLOWANCE								\$3,481
								\$365,502
NET OPERATING INCOME (NOI)								\$603,790
CAPITALIZATION								
OVERALL RATE								7.50%
TAX RATE (pay 2014)								1.95%
BUILT-UP RATE								9.45%
CAPITALIZED VALUE								\$6,389,316
LESS PERSONAL PROPERTY								\$1,000 per Unit
								\$105,000
INDICATED VALUE VIA INCOME APPROACH								\$6,284,316
								ROUNDED
INDICATED VALUE PER UNIT								\$6,284,000
								PER UNIT
								\$59,848

Mass Appraisal Model

	A	B	C	D	E	F	G	H	I
1									
2	Income Pro Forma - 2014 Assessment								
3	Sample Mass Appraisal								
4	Old Cedar Ave S								
5	Bloomington, MN								
6									
7									
9									
10									
11	# of UNITS	Model Name	Estimated Unit Type	Estimated SF per Unit	Total SF		Economic Market Rent per/Month	Economic Market Rent per SF	Monthly Economic Market Rent
14	2		Efficiency	400	800		\$515	\$1.29	\$1,030
15	73		1 Bedroom	875	63,875		\$715	\$0.82	\$52,195
16	27		2 Bedrooms	1,150	31,050		\$945	\$0.82	\$25,515
17	3		3 Bedrooms	1,650	4,950		\$1,300	\$0.79	\$3,900
18									
19	105	Total Units			100,675	NRA		\$0.82	\$82,640
20									
21	50	Garages					\$30		\$1,500
22									
23	Monthly Market Rent								
24	Annual Market Rent								
25									\$84,140
									\$1,009,680

Floor Plans	Property Details	★ Ratings and Reviews	Moving Center			
▼ Floor Plan Options (4)						
FLOOR PLAN	BED	BATH	RENT	SQ FT	DEPOSIT	AVAILABILITY
Studio	studio	1	\$515	400		CHECK AVAILABILITY
1 Bedroom	1	1	\$600 - \$715	875	\$300	CHECK AVAILABILITY
2 Bedroom	2	1	\$945 - \$999	1150	\$350	CHECK AVAILABILITY

Mass Appraisal Model

CAPITALIZATION PROCESS			
POTENTIAL GROSS INCOME (PGI)			\$1,009,680
LESS: VACANCY & COLLECTION LOSS % OF PGI		5.00%	(\$50,484)
OTHER INCOME:		1.00% of PGI	\$10,097
EFFECTIVE GROSS INCOME (EGI)			\$969,293
LESS: ANNUAL OPERATING EXPENSES		% OF EGI 35.00%	\$/ Unit \$3,231 \$339,252
LESS: ANNUAL RESERVES FOR REPLACEMENT	\$250/unit	<u>2.71%</u>	<u>\$250</u> \$26,250
TOTAL ANNUAL ALLOWANCE		37.71%	\$3,481 \$365,502
NET OPERATING INCOME (NOI)			\$603,790
<u>CAPITALIZATION</u>			
OVERALL RATE		7.50%	
<u>TAX RATE (pay 2014)</u>		<u>1.95%</u>	
BUILT-UP RATE		9.45%	
CAPITALIZED VALUE			\$6,389,316
LESS PERSONAL PROPERTY		<u>\$1,000</u> per Unit	\$105,000
INDICATED VALUE VIA INCOME APPROACH			\$6,284,316

Mass Appraisal Model



- Test Your Model!
 - ▣ Listings
 - ▣ Sales
 - ▣ Appeals

GRM/GIM Model

Project Name					Unit		Sale Price			
Property ID#	PID	Address	Year Built	Units	Mix	Sale Date	Sale Price	Per Unit	GRM	AVG
7 Unit	17-027-24-44-0001	2301 Maple Ave S	1961	7	1BR-6; 2BR-1	11/10/2016	\$490,000	\$70,000	9.35	
4-Plex	10-027-24-31-0023	10 92nd St W	1959	4		06/30/2016	\$300,000	\$75,000	7.87	
Washburn Circle 4 Plex	05-027-24-13-0012	8003 Washburn Cir S	1963	4		06/10/2016	\$447,000	\$111,750	9.55	
11 Unit Building	15-027-24-24-0005	9730 Nicollet Ave S	1963	11		04/29/2016	\$950,000	\$86,364	8.27	
4-Plex	11-027-24-14-0068	8812 Old Cedar Ave S	1962	4		04/04/2016	\$330,000	\$82,500	7.53	
4-Plex	11-027-24-14-0079	8807 18th Ave S	1960	4	1BR-1; 2BR-3	12/15/2015	\$295,000	\$73,750	7.62	
4-Plex	10-027-24-31-0013	9110 Nicollet Ave S	1960	4		11/12/2015	\$320,000	\$80,000	7.96	
4-Plex	03-027-24-31-0022	8228 Nicollet Ave S	1959	4		09/01/2015	\$323,470	\$80,868	7.6	
4-Plex	11-027-24-14-0071	8836 Old Cedar Ave S	1963	4	1BR-1; 2BR-3	08/28/2015	\$240,000	\$60,000	6.3	
4-Plex	11-027-24-14-0072	8842 Old Cedar Ave S	1963	4	1BR-1; 2BR-3	02/27/2015	\$230,000	\$57,500	6.04	
6 Unit	10-027-24-31-0005	9040 Nicollet Ave S	1966	6	2BR-4; 3BR-2	10/31/2014	\$595,000	\$99,167	8.71	
									7.9	AVG

	Gross Rent Multiplier Range		
	Low	High	Avg
	7.5	8.5	7.9
Gross Rent Indicated Value	\$51,000	\$51,000	\$51,000
PP Deduct Value	\$382,500	\$433,500	\$402,900
	\$2,500	\$2,500	\$2,500
Value	\$380,000	\$431,000	\$400,000

GRM/GIM Model

2015 Apartment Comps

Class B



Povence Luxury Apts
Burnsville



Thomas Lake Pointe
Eagan



Louisiana Oaks
Saint Louis Park



Valley Creek Apartments
Woodbury

Year Built	2001	1987	2001	1987
Sale Date	09/03/2015	01/14/2015	04/30/2015	05/14/2015
Units	157	216	200	402
Sale Price	\$20,150,000	\$31,000,000	\$35,215,292	\$54,250,000
Sale Price / Unit	\$128,344	\$143,519	\$176,076	\$134,950
Cap Rate	5.50%	5.96%	5.25%	5.50%
GRM	9.29	9.99	10.62	10.24
Avg Unit Size	1029	1060	1031	939
Avg Rent/Unit	\$1,151	\$1,197	\$1,382	\$1,098
Avg Rent /SF	\$1.12	\$1.13	\$1.13	\$1.17
Notes	5.9% Year 1 pro forma		TIF Note = \$3,884,708 Total SP = \$39,100,000	

Question & Answer



Case Study

Case Study

MULTI-FAMILY PRO FORMA--CASE STUDY					
INCOME PROJECTIONS:					
Unit Type	# of Units	Projected Monthly Rent		# of Months	Projected Annual Rent
1-BR/1-BA Unit (600 Square Feet)	x		x	12	=
2-BR/2-BA Unit (825 Square Feet)	x		x	12	=
Projected Gross Apartment Income	x		x	12	=
Less: Vacancy and Credit Loss Allowance @					
Effective Gross Apartment Income					
Effective Gross Miscellaneous Income					
Rent Concessions:					
TOTAL EFFECTIVE GROSS INCOME - ALL SOURCES					
TOTAL OPERATING EXPENSES					
NET OPERATING INCOME					
DIRECT CAPITALIZATION					
Net Operating Income					
Capitalization Rate					
Effective Tax Rate					
Loaded Cap Rate (Total)					
FEE SIMPLE MARKET VALUE INDICATION					
ROUNDED TO:					
Per Unit					



MAAO

Minnesota Association
of Assessing Officers

**Allocation of Real Estate
Value in Assisted Living
Facilities**

Brad Moore, MAI
Principal
Nicollet Partners, Inc.

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CIA Valuations Committee

Overview

- Going Concern and It's Components
- Market Trends for Assisted Living
- Allocation of Real Estate Value in Assisted Living
 - Income Approach: Case Study
 - Sales Comparison Approach
 - Cost Approach

CIA Valuations Committee

Going Concern: Terms & Concepts

Definition of Going Concern

The Appraisal of Real Estate, 14th Ed.

Going concern. All tangible and intangible assets of an established and operating business with an indefinite life.⁵

- Company is expected to continue operating well into the future.
- Business assets, both tangible and intangible, are sold in aggregate to a single purchaser.

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Going Concern: Terms & Concepts

Definition of Going Concern Value

The Dictionary of Real Estate Appraisal, 6th Ed.

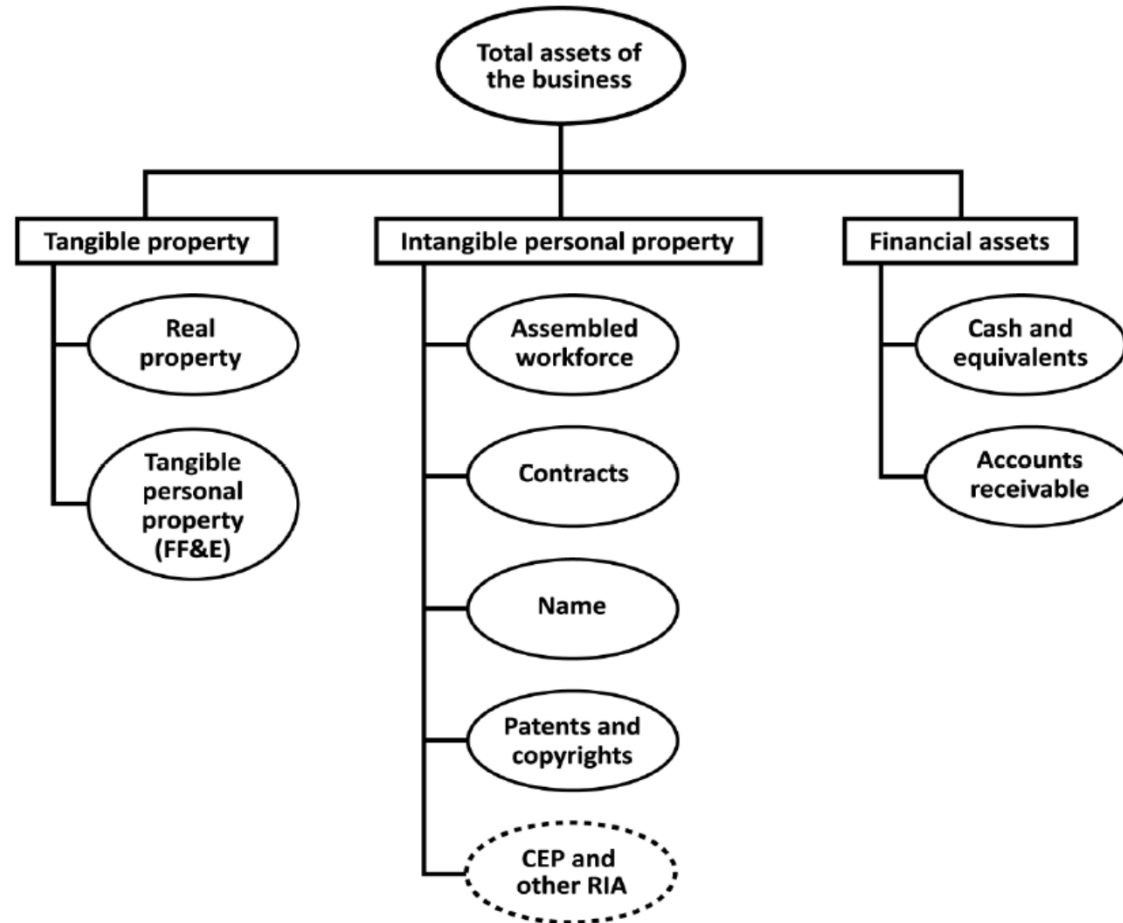
Going-concern value. *An outdated label for the market value of all the tangible and intangible assets of an established and operating business with an indefinite life, as if sold in aggregate; more accurately termed the market value of the going concern or market value of the total assets of the business. See also market value of the going concern.*

Market Value of the Total Assets of the Business
(MVTAB)

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Going Concern: Terms & Concepts

III. Components of a Going Concern or Business



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Going Concern: Terms & Concepts

Tangible Property

Tangible property. *Property that can be perceived with the senses; includes land, fixed improvements, furnishings, equipment and physical supplies, inventory, and merchandise. Some accounting sources indicate that tangible property includes all property not properly classified as identifiable intangible assets or goodwill. On that basis, tangible property includes real estate, personal property, and working capital assets such as cash, cash equivalents, accounts receivable, supplies, and inventory, although cash and accounts receivable are not themselves tangible per se.*

- 1) Real Property
- 2) Tangible Personal Property (FF&E)

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Going Concern: Terms & Concepts

1) Real Property

Real Estate or the bricks and sticks

- Apartments
- Office
- Industrial

We Understand This Concept!!

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Going Concern: Terms & Concepts

2) Tangible Personal Property (FF&E)

- All tangible business assets that are not real property as by default are tangible personal property.
- Furnishings (table/chairs), Office Equipment (computers), Inventory (medical supplies), Artwork, Bus

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Going Concern: Terms & Concepts

3) Intangible Personal Property

Intangible property (Intangible assets). “Nonphysical assets, including but not limited to franchises, trademarks, patents, copyrights, goodwill, equities, securities, and contracts as distinguished from physical assets such as facilities and equipment.” (USPAP, Definitions section)

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Going Concern: Terms & Concepts

Examples of Intangible Personal Property

- Assembled workforce: Trained staff/skilled labor
 - Nurses/Home Health Aides
 - Cooks/Servers
- Contracts: non-realty
 - State License
 - Third Party Home Care Contract
 - Sale/Leaseback
- Name: reputation of a business
 - Hilton, Holiday Inn, Etc.

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Going Concern: Terms & Concepts

Why are these terms and concepts important?

- Recognize Intangible Assets
- Allow us to ask better questions about the business
- Help us to make informed decisions

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Market Trends for Assisted Living

Income Growth

- Housing rates: 2% to 4% annual increase
- Health care service rates: Difficult to track
- EGI Growth: 3% to 6%/yr for Stabilized Properties

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Market Trends for Assisted Living

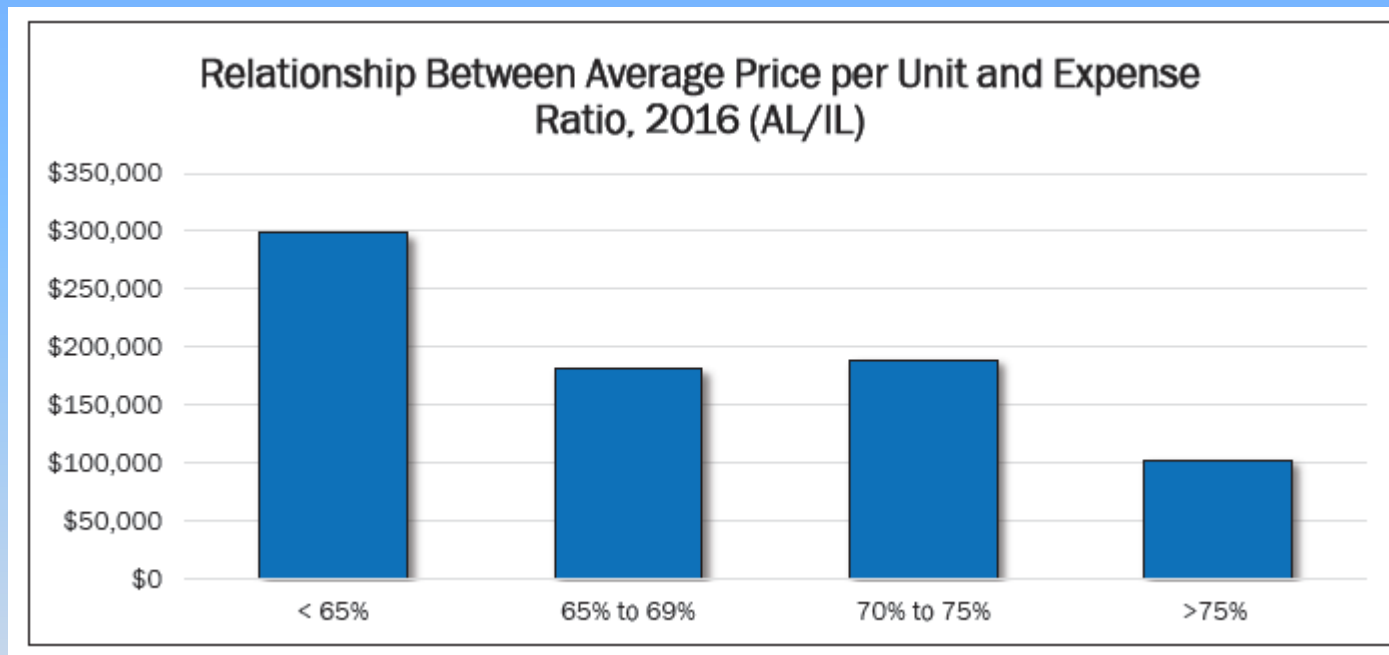
Operating Expenses

- Expense Ratios:
 - <60%: typically limited amount of services
 - 60% to 65%: well performing, mostly private pay
 - 65% to 69%: more typical for assisted living
 - 70% to 75%: higher acuity and Medicaid
 - >75%: Specialty care or non-stabilized
- These are very generalized. Ratios are misleading!

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Market Trends for Assisted Living

Operating Expenses

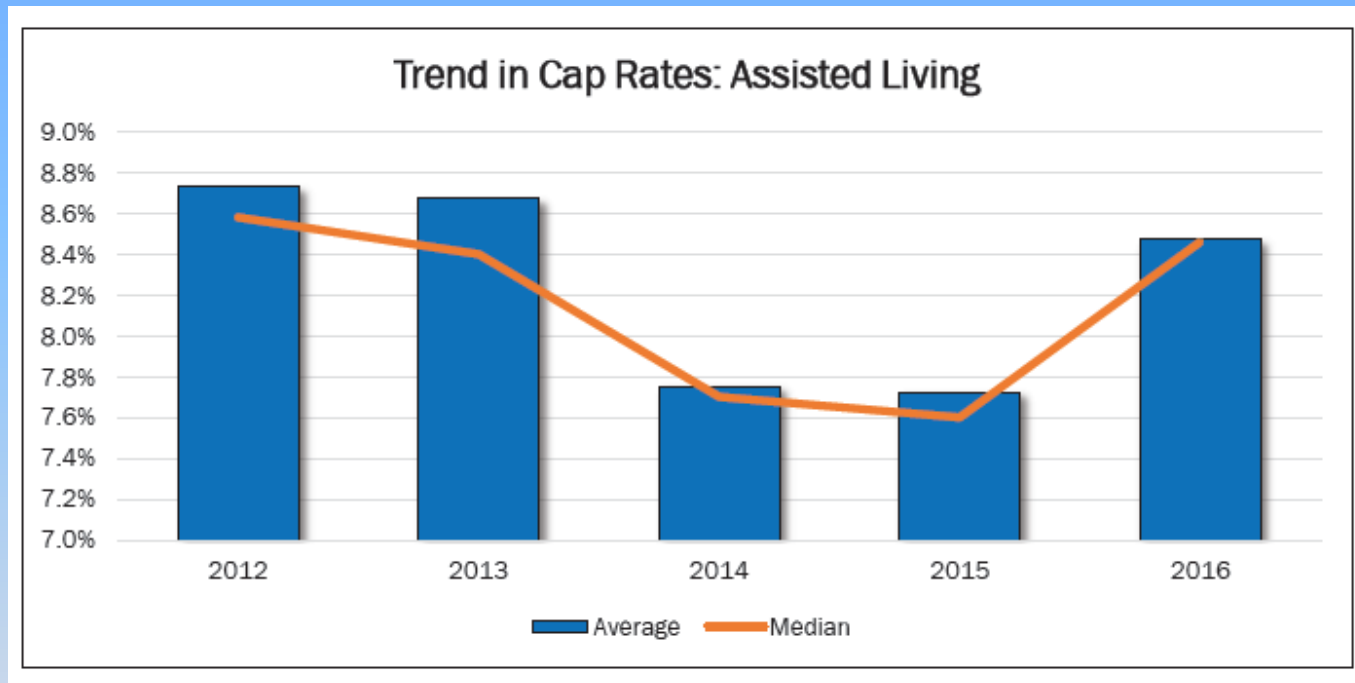


Source: Senior Care Acquisition Report; Twenty-Second Edition, 2017

- There is a correlation between price paid and OER

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Market Trends for Assisted Living Cap Rates



Source: Senior Care Acquisition Report; Twenty-Second Edition, 2017

- Increase in Average Cap Rate
- More sales of “Value-add” properties, fewer “A” quality sales

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Market Trends for Assisted Living

Cap Rates: Class A

SCAR Senior Sales - Over \$200,000 per bed									
SCAR	No. of Units	Occupancy %	Date of	Type of	NOI	Sale Price	Overall	Equity Div.	
Sale #	Name/Location	Total	% Medicaid	Sale	NOI	NOI/Unit	\$/Unit	Cap Rate	Rate
1	The Arbors at Ranch Penasquite San Diego, CA	87 Yr. Blt. ±1999	90% NA	Jan-14	Trailing 12	\$1,500,000 \$17,241	\$19,500,000 \$224,138	7.69%	11.99%
2	Arbor Terrace of East Cobb Marietta, Georgia	90 Yr. Blt. 2000	100% NA	Mar-14	Trailing 12	\$1,500,000 \$16,667	\$21,250,000 \$236,111	7.06%	9.46%
3	Sudley Manor Manassas, VA	72 Yr. Blt. 2000	96% NA	Jul-14	Proforma	\$1,300,000 \$18,056	\$15,200,000 \$211,111	8.55%	15.43%
4	Grand View Alzheimer's Care Peoria, IL	66 Yr. Blt. 2012	NA NA	Nov-14	Trailing 12	\$1,224,600 \$18,555	\$15,700,000 \$237,879	7.80%	12.42%
5	Hidden Lake Canton, Georgia	49 Yr. Blt. 2014	100% NA	Dec-14	Proforma	\$1,025,000 \$20,918	\$14,550,000 \$296,939	7.04%	9.94%
6	Benton House of Shoal Creek Kansas City, MO	88 Yr. Blt. 2012	91% NA	Feb-15	Proforma	\$1,995,000 \$22,670	\$28,500,000 \$323,864	7.00%	9.22%
7	Seven Lakes Memory Care Loveland, CO	48 Yr. Blt. 2011	NA 0	Mar-15	Proforma	NA	\$13,050,000 \$271,875		
8	Inn at Fairfield Village Lancaster, OH	92 Yr. Blt. 2006	NA 20%	Jul-15	Trailing 12	\$1,680,000 \$18,261	\$21,000,000 \$228,261	8.00%	13.22%
Averages						\$18,910	\$253,772	7.59%	11.67%

Source: Senior Care Acquisition Report

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Market Trends for Assisted Living

Cap Rates: Outstate Locations

Summary of Local Sales (Upper Midwest)									
SCAR	No. of Units	Occupancy %	Date of	Type of	NOI	Sale Price	Overall	Equity Div.	
Sale #	Name/Location	Total	% Medicaid	Sale	NOI	NOI/Unit	\$/Unit	Cap Rate	Rate
1	Wedgewood Gardens BransonWest, MO	23 Yr. Blt. 1996	100% NA	Mar-15	Trailing 12	\$241,000 \$10,478	\$2,300,000 \$187,054	10.48%	23.13%
2	Bridgeway Estates Little Falls, MN	42 Yr. Blt.: NA	93% Very little	Mar-14	Trailing 12	\$280,000 \$6,667	\$3,500,000 \$129,726	8.00%	13.22%
3	The Continental at St. Joseph's Centerville, IA	51 Yr. Blt. 2002	85% 8%	Sep-14	Proforma	\$488,457 \$9,578	\$5,365,000 \$105,196	9.10%	17.64%
4	The Legends at Heritage Sartell, MN	121 Yr. Blt. 2009	83% 60%	Oct-13	Proforma	\$1,670,565 \$13,806	\$19,170,000 \$158,430	8.71%	16.62%
5	Willow Pointe AL Verona, WI	68 Yr. Blt. 1998	97% NA	Dec-13	Proforma	\$1,039,166 \$15,282	\$12,000,000 \$176,471	8.66%	15.86%
6	The Waterford at Oshkosh Osahkosh, WI	98 Yr. Blt. 2008/13	95% 50%	Aug-14	Proforma	\$1,458,061 \$14,878	\$17,125,000 \$174,745	8.51%	15.82%
7	Jackson Crossings Jackson, WI	54 Yr. Blt. 2006	85% 5%	Nov-14	Proforma	\$615,214 \$11,393	\$7,000,000 \$129,630	8.79%	16.92%
8	Whispering Oaks Ellendale, MN	32 Yr. Blt. 2004	100% 25%	Nov-14	Trailing 6	\$211,625 \$6,613	\$2,500,000 \$78,125	8.47%	15.62%
Averages						\$11,087	\$142,422	8.84%	16.85%

Source: SCAR & Nicollet Partners, Inc.

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Market Trends for Assisted Living

Cap Rates: Sources

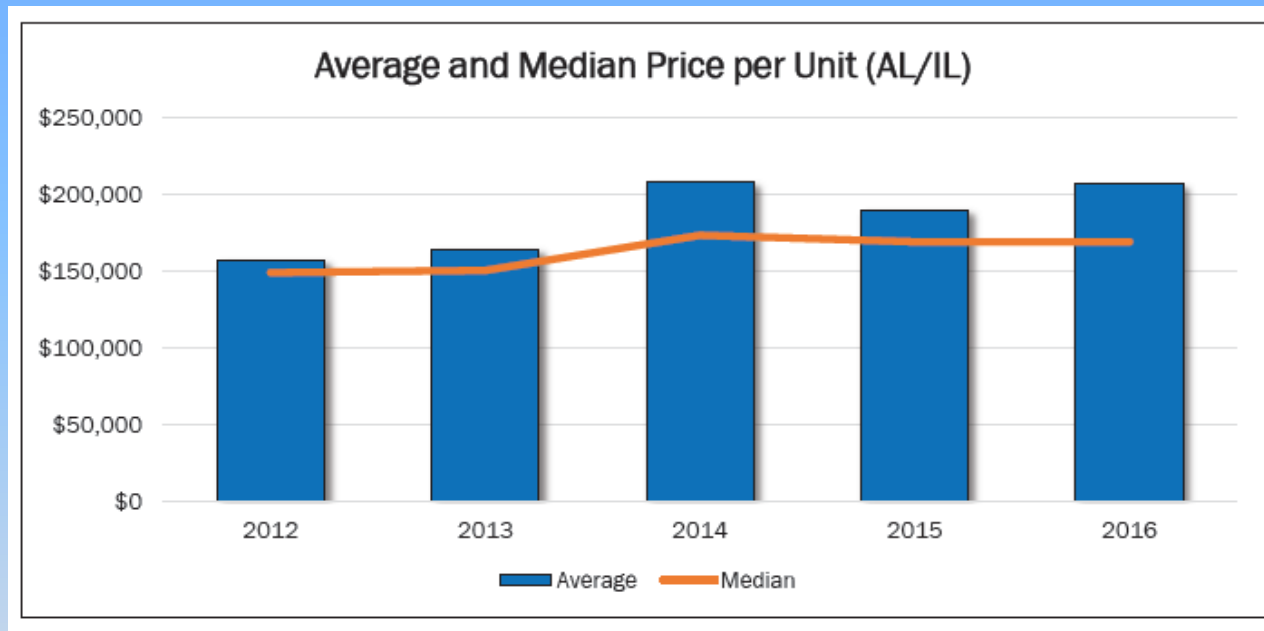
- Senior Care Acquisition Report: SCAR
- NIC Investor Survey
- Brokers/Appraisers
- Market Extracted Sales

- Assisted Living Cap Rates are Difficult to Come By

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Market Trends for Assisted Living

Sales Trends: AL/IL Combined



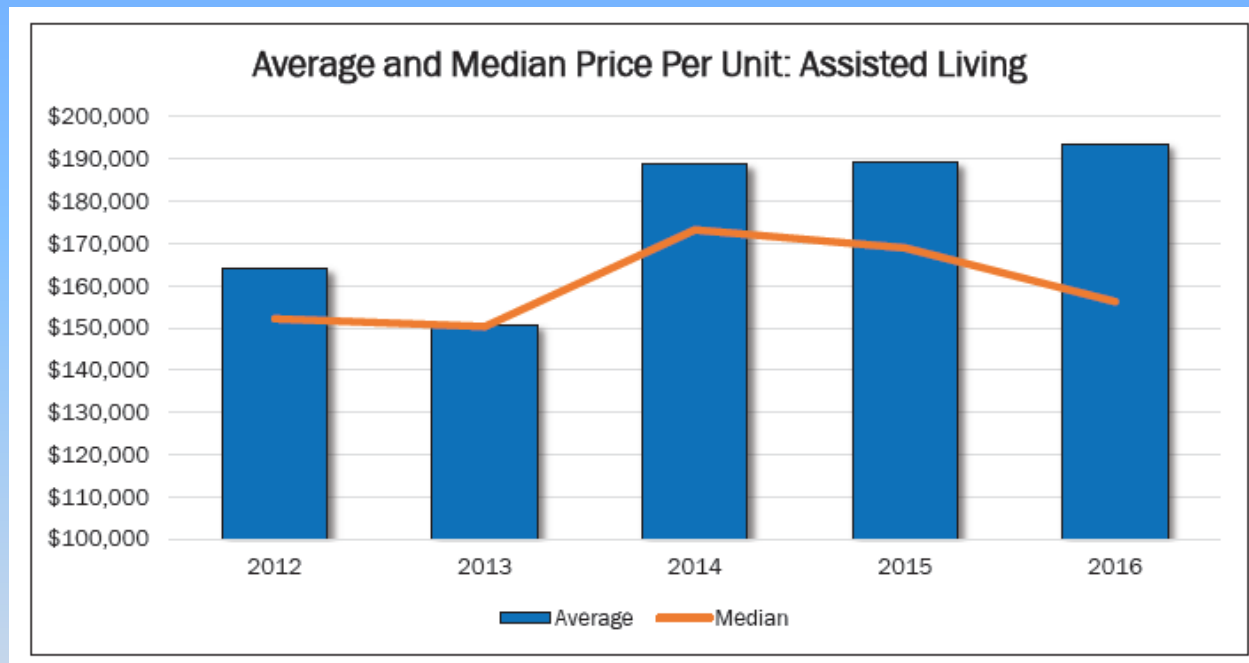
Source: Senior Care Acquisition Report; Twenty-Second Edition, 2017

- 2016 sales are up 9% from 2015, but down 1% from 2014.
- What is the correct trend?

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Market Trends for Assisted Living

Sales Trends: Assisted Living



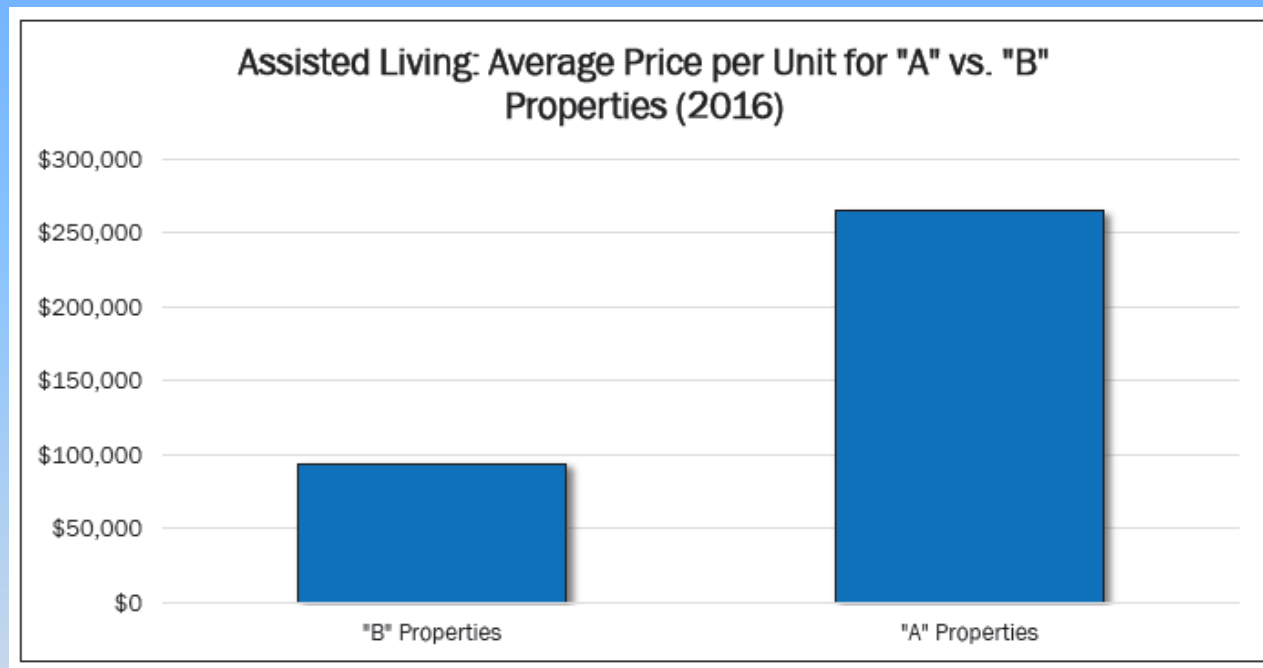
Source: Senior Care Acquisition Report; Twenty-Second Edition, 2017

- 2016 sales reflect higher proportion of memory care than previous years
- What is the correct trend?

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Market Trends for Assisted Living

Sales Trends: "A" vs. "B"



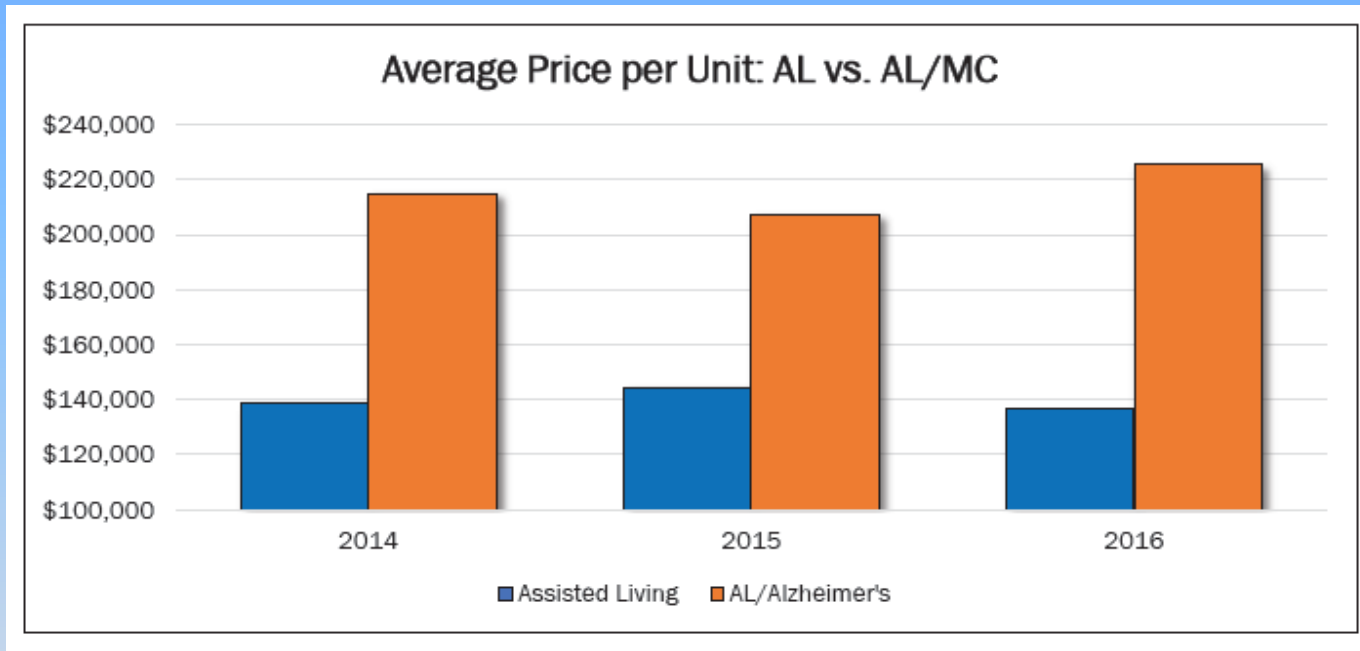
Source: Senior Care Acquisition Report; Twenty-Second Edition, 2017

- A properties: 7% value increase, 8% cap rate, 91% vacancy rate, 67% OER
- B properties: value decline, 9% cap rate, 84% vacancy rate, 77% OER

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Market Trends for Assisted Living

Sales Trends: AL vs. AL/MC



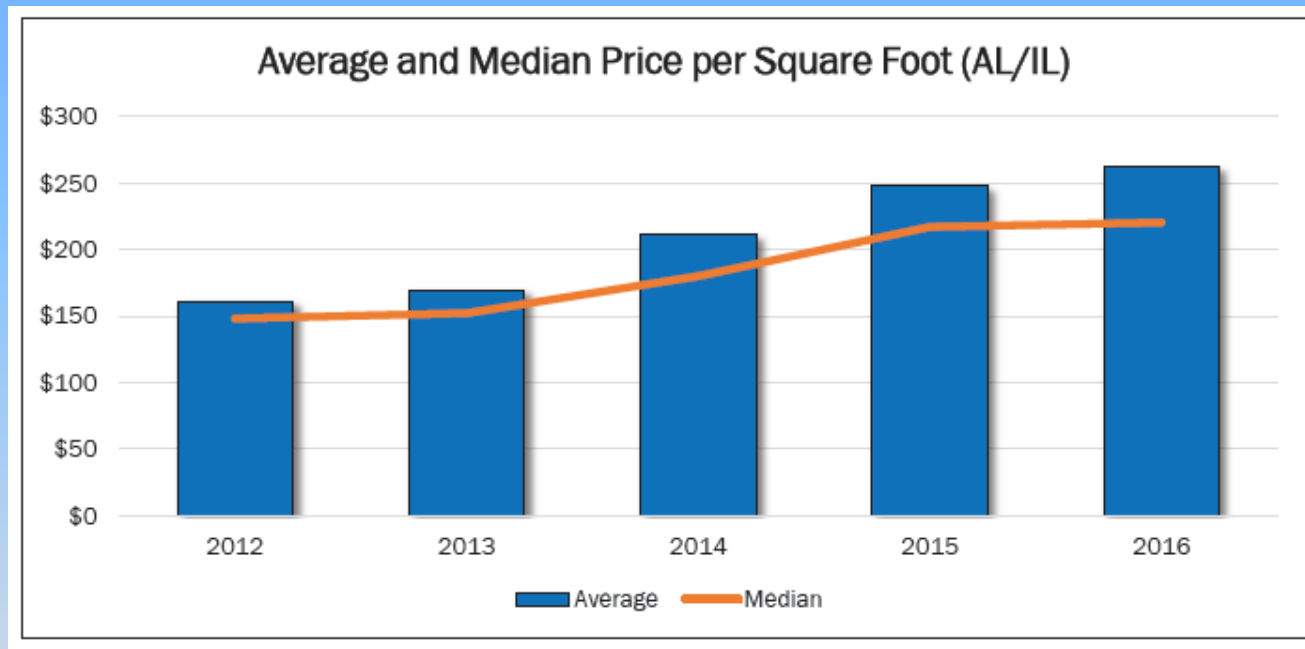
Source: Senior Care Acquisition Report; Twenty-Second Edition, 2017

- Higher sale prices for facilities with memory care
- Higher housing rates for memory care

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Market Trends for Assisted Living

Sales Trends: PSF (AL/IL)



Source: Senior Care Acquisition Report; Twenty-Second Edition, 2017

- Growing number of sales with memory care
- Memory care sells for higher prices per unit and higher price per sq. ft.

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Market Trends for Assisted Living

Sales Trends: Conclusions

- Income and expenses are increasing
- Interest rates and cap rates are near historic lows
- Strong investor demand and record sale prices
- MVTAB Sale Prices support cost of new construction
- New Construction throughout Minnesota

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Market Trends for Assisted Living

What does this mean for Assessors?

- Every AL facility is uniquely different and uniquely operated.
- If you have appraised 1 assisted living facility, you have appraised 1 assisted living facility.
- This makes it challenging for mass appraisal. Fortunately, allocation of the RE value doesn't have to be complicated.

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Allocation of Real Estate Value

Case Study: Housing Rates

- Housing Service Contract Rates are not the same as rent.

SUMMARY OF UNIT MIX & SIZE						
<u>Unit Type</u>	<u>Unit Code</u>	<u># of Units</u>	<u># of Beds</u>	<u>Gross Unit Size (Sq. Ft.)</u>	<u>Total Gross Sq.ft.</u>	<u>Housing Serv. Asking Rate</u>
<u>Assisted Living</u>						
1 BR/1 bath	A	24	24	528	12,672	\$2,005
1 BR/1 bath	B	3	3	644	1,932	\$2,040
1 BR/1 bath	C	2	2	780	1,560	\$2,250
1 BR/1 bath/den	D	<u>3</u>	<u>3</u>	<u>1,000</u>	<u>3,000</u>	\$2,530
Subtotal		32	32	599	19,164	
<u>Memory Care</u>						
Shared Unit	A - MC	1	2	321	321	\$1,300
1 BR/1 bath	B - MC	6	6	528	3,168	\$2,400
1 BR/1 bath	C - MC	<u>1</u>	<u>1</u>	<u>644</u>	<u>644</u>	\$2,450
Subtotal		8	9	517	4,133	
Project Totals		40	41	582	23,297	

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Allocation of Real Estate Value

Case Study: Housing Rates

- Housing Service Contract Rates include services

Assisted Living - Included in the Basic Monthly Rent:

- Private apartment with full kitchen (*dishwashers at Pines only*)
- One meal per day (noon)
- Daily snack
- Weekly light housekeeping
- Social, spiritual, & recreational programs
- Most utilities included: heat, electric, water, basic cable, and WiFi
- Daily "OK" check
- 24 hour response system
- Professionally owned & managed by Ecumen

INCLUDED IN YOUR MONTHLY FEE:

- 24-hour, on-site care staff
- Private apartment with private bath & kitchen
- Three meals each day plus snacks
- Specialized social, physical, spiritual and recreational activities
- Most utilities (heat, electric, water and daily trash pickup)
- Basic cable television service
- Residential setting with secure access and environment
- Secure outdoor patio
- Weekly housekeeping
- Laundry and linen service as needed
- Full-time, licensed nurses
- RN on-call 24 hours/day
- Comfort checks around the clock
- Escorts to meals and activities
- Neighborhood dining

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Allocation of Real Estate Value

Case Study: Health Care Services

- Health care services are part of a home care business

Level 1:

Morning and evening dressing and grooming including supervision, cues and oversight
Medication Management
Escort to and from meals and activities
Verbal reminders for bathroom usage
Reassurance checks
Bathing assistance, supervision, cues and oversight 2 times per week
Cognitive support i.e.: redirection and orientation
Monitoring of vital signs and weight, monthly
Bed making

Level 2:

All Level 1 services, plus:

Step-by-step limited physical assistance with dressing and grooming, morning and evening
Occasional assistance with incontinence cares
Mobility and transferring assistance requiring stand-by assistance

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Allocation of Real Estate Value

Case Study: Gross Income Projection

- Gross Potential Income is very high

<i>HOUSING INCOME PROJECTION - PGI</i>										
<i>Type of Unit</i>	<i>Unit Code</i>	<i># of Beds</i>	<i>Size of Unit</i>	<i>No. of Private Pay Beds</i>	<i>Est. Base Housing Serv. Rates</i>	<i>Total Annual PP Income</i>	<i>No. of Medicaid Beds</i>	<i>Monthly GRH Rate</i>	<i>Total Annual GRH Income</i>	<i>Total Annual Housing Income x 12</i>
<i>Assisted Living</i>										
1 BR/1 bath	A	24	528	18	\$2,005	\$433,080	6	\$867	\$62,424	\$495,504
1 BR/1 bath	B	3	644	3	\$2,040	\$73,440	0	\$867	\$0	\$73,440
1 BR/1 bath	C	2	780	2	\$2,250	\$54,000	0	\$867	\$0	\$54,000
1 BR/1 bath/den	D	3	1,000	3	\$2,530	\$91,080	0	\$867	\$0	\$91,080
Subtotal		32		26		\$651,600	6		\$62,424	\$714,024
Subtotal - \$/bed						\$25,062			\$10,404	\$22,313
<i>Memory Care</i>										
Shared Unit	A- MC	2	321	1	\$1,300	\$15,600	1	\$867	\$10,404	\$26,004
1 BR/1 bath	B- MC	6	528	6	\$2,400	\$172,800	0	\$867	\$0	\$172,800
1 BR/1 bath	C- MC	1	644	1	\$2,450	\$29,400	0	\$867	\$0	\$29,400
Subtotal		9		8		\$217,800	1		\$10,404	\$228,204
Subtotal - \$/bed						\$27,225			\$10,404	\$25,356
Project Totals		41		34		\$869,400	7		\$72,828	\$942,228
\$/bed (total)						\$25,571			\$10,404	\$22,981

CIA Valuations Committee

Allocation of Real Estate Value

Case Study: Gross Income Projection

- Health Care Income can vary greatly

<i>HEALTH SERVICE INCOME PROJECTION - PGI</i>										
<i>Type of Unit</i>	<i>Unit Code</i>	<i># of Beds</i>	<i>Size of Unit</i>	<i>No. of Private Pay Beds</i>	<i>Add'l Health Service Inc. Per Bed</i>	<i>Total Annual Rent x 12</i>	<i>No. of Medicaid Waiver Beds</i>	<i>Medicaid Waiver Inc. Per Bed</i>	<i>Total Annual Rent x 12</i>	<i>Total Annual Service Income x 12</i>
<i><u>Assisted Living</u></i>										
1 BR/1 bath	A	24	528	18	\$400	\$86,400	6	\$1,050	\$75,600	\$162,000
1 BR/1 bath	C	2	780	2	\$400	\$9,600	0	\$1,050	\$0	\$9,600
1 BR/1 bath/den	D	3	1,000	3	\$400	\$14,400	0	\$1,050	\$0	\$14,400
Subtotal		29		23		\$110,400	6		\$75,600	\$186,000
Subtotal - \$/bed						\$4,800			\$12,600	\$6,414
<i><u>Memory Care</u></i>										
Shared Unit	A - MC	2	321	1	\$2,300	\$27,600	1	\$5,000	\$60,000	\$87,600
1 BR/1 bath	B - MC	6	528	6	\$2,300	\$165,600	0	\$5,000	\$0	\$165,600
1 BR/1 bath	C - MC	1	644	1	\$2,300	\$27,600	0	\$5,000	\$0	\$27,600
Subtotal		9		8		\$220,800	1		\$60,000	\$280,800
Subtotal - \$/bed						\$27,600			\$60,000	\$31,200
Project Totals		38		31		\$331,200	7		\$135,600	\$466,800
\$/bed (total)						\$10,684			\$19,371	\$12,284

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Allocation of Real Estate Value

Case Study: Operating Expenses

- Payroll and Senior Services are at 50% to 60% of EGI.
- Payroll and Senior Services represent 75% to 85% of the total operating expenses at a given property.
- Senior Services include: activities, dietary, home health aides, housekeeping, laundry, transportation, and skilled nursing.

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Allocation of Real Estate Value

Case Study: Operating Expenses

Expense Comparables

Eff. Gross Income (\$/unit)	\$35,207	\$31,113	\$32,321	\$38,763	\$32,356
Advertising	\$681	\$484	\$109	\$243	\$310
Management	\$0	\$1,555	\$0	\$568	\$865
Mgmt. Fee as % of EGI	0.00%	5.00%	0.00%	1.46%	2.67%
Administrative	\$1,291	\$945	\$1,119	\$334	\$905
Elevator	\$103	\$67	\$0	\$0	\$28
Fuel	\$0	\$0	\$0	\$0	\$0
Electric	\$641	\$674	\$556	\$537	\$590
Water and Sewer	\$310	\$369	\$241	\$89	\$230
Gas	\$238	\$214	\$202	\$234	\$225
Trash Removal	\$50	\$73	\$77	\$0	\$74
Payroll/Senior Services	\$18,827	\$15,447	\$19,933	\$22,716	\$17,221
Payroll/Services as % of EGI	53.48%	49.65%	61.67%	58.60%	53.22%
Legal/Audit	\$270	\$14	\$24	\$201	\$105
Insurance	\$467	\$187	\$274	\$222	\$239
Grounds and Security	\$178	\$177	\$60	\$0	\$96
Decorating	\$8	\$112	\$0	\$0	\$20
Repairs & Maint.	\$1,396	\$551	\$321	\$1,370	\$792
Exterminating	\$15	\$16	\$0	\$0	\$11
Other	\$0	\$0	\$0	\$0	\$0
Expenses (before Reserves & Taxes)	\$24,476	\$20,885	\$22,915	\$26,515	\$21,712
Replacement Reserves	\$300	\$300	\$300	\$300	\$300
Subtotal+Trend+RR	\$24,776	\$21,185	\$23,215	\$26,815	\$22,012
Taxes/Real Estate	\$796	\$969	\$683	\$913	\$951
Total Expenses	\$25,572	\$22,154	\$23,898	\$27,728	\$22,963

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Allocation of Real Estate Value

Case Study: Operating Expenses

Health Care Service Expenses

HEALTH CARE SERVICE EXPENSES								
	<i><u>\$/bed</u></i>	<i><u>% of EGI</u></i>	<i><u>\$/bed</u></i>	<i><u>% of EGI</u></i>	<i><u>\$/bed</u></i>	<i><u>% of EGI</u></i>	<i><u>\$/bed</u></i>	<i><u>% of EGI</u></i>
<i>EGI</i>	<i>\$36,257</i>		<i>\$31,108</i>		<i>\$33,038</i>		<i>\$37,625</i>	
Payroll & Benefits	<i>\$5,656</i>	<i>15.6%</i>	<i>\$1,383</i>	<i>4.4%</i>	<i>\$4,578</i>	<i>13.9%</i>	<i>\$19,396</i>	<i>51.6%</i>
<i>Activities</i>	<i>\$542</i>	<i>1.5%</i>	<i>\$0</i>	<i>0.0%</i>	<i>\$966</i>	<i>2.9%</i>	<i>\$0</i>	<i>0.0%</i>
<i>Dietary</i>	<i>\$2,643</i>	<i>7.3%</i>	<i>\$3,669</i>	<i>11.8%</i>	<i>\$3,138</i>	<i>9.5%</i>	<i>\$1,917</i>	<i>5.1%</i>
<i>Home Health Aide</i>	<i>\$7,729</i>	<i>21.3%</i>	<i>\$6,900</i>	<i>22.2%</i>	<i>\$7,089</i>	<i>21.5%</i>	<i>\$1,176</i>	<i>3.1%</i>
<i>Housekeeping</i>	<i>\$111</i>	<i>0.3%</i>	<i>\$1,041</i>	<i>3.3%</i>	<i>\$326</i>	<i>1.0%</i>	<i>\$0</i>	<i>0.0%</i>
<i>Laundry/Linen</i>	<i>\$9</i>	<i>0.0%</i>	<i>\$0</i>	<i>0.0%</i>	<i>\$26</i>	<i>0.1%</i>	<i>\$0</i>	<i>0.0%</i>
<i>Transportation</i>	<i>\$197</i>	<i>0.5%</i>	<i>\$0</i>	<i>0.0%</i>	<i>\$0</i>	<i>0.0%</i>	<i>\$0</i>	<i>0.0%</i>
<i>Skilled Nursing</i>	<i>\$2,127</i>	<i>5.9%</i>	<i>\$2,453</i>	<i>7.9%</i>	<i>\$3,958</i>	<i>12.0%</i>	<i>\$0</i>	<i>0.0%</i>
Services	<i>\$13,358</i>	<i>36.8%</i>	<i>\$14,063</i>	<i>45.2%</i>	<i>\$15,503</i>	<i>46.9%</i>	<i>\$3,093</i>	<i>8.2%</i>
Total Salaries & Services*	<i>\$19,014</i>	<i>52.4%</i>	<i>\$15,446</i>	<i>49.7%</i>	<i>\$20,081</i>	<i>60.8%</i>	<i>\$22,489</i>	<i>59.8%</i>

Salaries are the largest expense for each senior service.

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Allocation of Real Estate Value

Case Study: Allocated RE Rent

- Method 1: Rent Comparison
 - Apartments
 - Age-restricted apartments
 - Senior IL communities (stand alone facility, not part of a campus)
- Method 2: Extract out the health care from the Housing Rate
 - Difficult to extract health care portion
 - Works best when you have rooms (no bathrooms or kitchens)

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Allocation of Real Estate Value

Case Study: Allocated RE Rent

- Rent adjustment considerations
 - Landlord vs. tenant paid utilities
 - Units without kitchens or bathrooms
 - Super adequate project amenities (i.e., commercial kitchen)
 - Senior Campus premium?
 - What are the alternative rental options? What is the opportunity cost for residents
- In the Allocation of Real Estate Value, most focus should be put on rental rates.

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Allocation of Real Estate Value

Case Study: Allocated RE Rent

<i>HOUSING INCOME PROJECTION - PGI</i>						
<i>Type of Unit</i>	<i>Unit Code</i>	<i># of Beds</i>	<i>Size of Unit</i>	<i>No. of Market Units</i>	<i>Appraiser's Estimated RE Rent</i>	<i>Total Annual PGI</i>
<i>Assisted Living</i>						
1 BR/1 bath	A	24	528	24	\$740	\$213,120
1 BR/1 bath	B	3	644	3	\$769	\$27,684
1 BR/1 bath	C	2	780	2	\$803	\$19,272
1 BR/1 bath/den	D	<u>3</u>	1,000	<u>3</u>	\$900	<u>\$32,400</u>
Subtotal		32		32		\$292,476
Subtotal - \$/bed						\$9,140
<i>Memory Care</i>						
Shared Unit	A - MC	2	321	2	\$329	\$7,902
1 BR/1 bath	B - MC	6	528	6	\$740	\$53,280
1 BR/1 bath	C - MC	<u>1</u>	644	<u>1</u>	\$769	<u>\$9,228</u>
Subtotal		9		9		\$70,410
Subtotal - \$/bed						\$7,823
Project Totals		41		41		\$362,886
\$/bed (total)						\$8,851

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Allocation of Real Estate Value

Case Study: Vacancy and Misc. Income

- Vacancy Rate
 - What would be typical for real estate in this market
 - Can it be different than Assisted Living (MVTAB Value)?
- Miscellaneous Income
 - Exclude business service income

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Allocation of Real Estate Value

Case Study: Allocated EGI

Allocation of the Income

INCOME	Real Estate Only			Business			MVT AB
	Units	Per Unit	Total	Units	Per Unit	Total	Total
<i>Assisted Living</i>	32			32			
Gross Potential Income		\$9,140	\$292,476		\$18,986	\$607,548	\$900,024
a. Less Vacancy as a %		5.00%	5.00%		5.00%	5.00%	5.00%
b. Less vacancy as a \$ Amount		-\$457	-\$14,624		-\$949	-\$30,377	-\$45,001
Effective Gross Unit Income		\$8,683	\$277,852		\$18,037	\$577,171	\$855,023
<i>Memory Care</i>	9			9			
Gross Potential Income (MC)		\$7,823	\$70,410		\$48,733	\$438,594	\$509,004
a. Less Vacancy as a %		5.00%	5.00%		22.50%	22.50%	22.50%
b. Less vacancy as a \$ Amount		-\$391	-\$3,521		-\$10,965	-\$98,684	-\$114,526
Effective Gross Unit Income (MC)		\$7,432	\$66,890		\$37,768	\$339,910	\$394,478
EGI - before miscellaneous income	41	\$8,408	\$344,742	41	\$22,368	\$917,081	\$1,249,501
Miscellaneous Adjustments		\$129	\$5,274		\$885	\$36,285	\$41,559
Total Effective Gross Income (EGI)		\$8,537	\$350,016		\$23,253	\$953,366	\$1,291,060

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Allocation of Real Estate Value

Case Study: Allocated Expenses

- Expenses: What is typical of an Apartment Property?
 - Advertising: can be very high for senior AL
 - Administrative: AL is very high. Landlord paid cable/phone/internet?
 - Utilities: Landlord paid vs. tenant paid?
 - Payroll/senior services: What is typical for apartments?
 - Insurance: Is there higher liability insurance for seniors & providing care?
- Operating Expense Ratios: test of reasonableness

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Allocation of Real Estate Value

Case Study: Allocated Expenses

EXPENSES	Per Unit	Total	Per Unit	Total	Total
1 Advertising	\$125	\$5,125	\$35	\$1,435	\$6,560
2 Management	5.00%	\$426.85	\$1,163	\$47,668	\$64,553
3 Administrative	\$500	\$20,500	\$400	\$16,400	\$36,900
4 Elevator	\$0	\$0	\$0	\$0	\$0
5 Fuel	\$0	\$0	\$0	\$0	\$0
6 Electric	\$675	\$27,675	\$0	\$0	\$27,675
7 Water and Sewer	\$280	\$11,480	\$0	\$0	\$11,480
8 Gas	\$285	\$11,685	\$0	\$0	\$11,685
9 Trash Removal	\$115	\$4,715	\$0	\$0	\$4,715
10 Payroll/Senior Services	\$550	\$22,550	\$17,465	\$716,065	\$738,615
11 Legal/Audit	\$60	\$2,460	\$10	\$410	\$2,870
12 Insurance	\$200	\$8,200	\$45	\$1,845	\$10,045
13 Grounds and Security	\$100	\$4,100	\$0	\$0	\$4,100
14 Decorating	\$0	\$0	\$0	\$0	\$0
15 Repairs & Maint.	\$500	\$20,500	\$100	\$4,100	\$24,600
16 Exterminating	\$15	\$615	\$0	\$0	\$615
17 Other	\$0	\$0	\$0	\$0	\$0
19 Replacement Reserve	\$250	\$10,250	\$50	\$2,050	\$12,300
20 Operating Expenses (before RE Taxes)	\$4,082	\$167,356	\$19,253	\$789,358	\$956,713
21 Taxes/Real Estate	\$988	\$40,492	\$0	\$1	\$40,492
Total Expenses	\$5,069	\$207,848	\$19,253	\$789,359	\$997,205
- as a % of EGI	59.38%	59.38%	82.80%	82.80%	77.24%
STABILIZED NET OPERATING INCOME	\$3,467	\$142,168	\$4,000	\$164,007	\$293,855

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Allocation of Real Estate Value

Case Study: Allocated Cap Rates

- Cap Rates
 - Real Estate Cap Rate
 - Implied Business Cap Rate
 - Overall Cap Rate (MVTAB)
- Test of Reasonableness
 - Price Per Unit
 - Price PSF of GBA
 - Allocated % of RE compared to the MVTAB

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Allocation of Real Estate Value

Case Study: Allocated Cap Rates

Market Value Conclusions					
	Real Estate Only		Business Value		MVTAB
	S/Unit	Total	S/Unit	Total	Total
Stabilized Net Operating Income		\$142,168		\$164,007	\$306,175
Capitalization Rate		<u>7.25%</u>		<u>11.71%</u>	<u>8.75%</u>
Estimated Value (W/ FF&E)		\$1,960,937		\$1,538,221	\$3,499,146
Less: FF&E		(\$50,000)		(\$140,000)	(\$190,000)
Market Value, as rounded	\$47,750	\$1,910,000	\$35,000	\$1,400,000	\$3,310,000
Sales Price Per SF of GBA		\$48			\$83
Allocated Percent of Total:		57.7%		42.3%	100.0%

Capitalization of NOI - Loaded Cap Rate - Real Estate Only		
Real Estate Only - Net Operating Income		\$142,168
Add: Projected Real Estate Taxes		<u>\$40,492</u>
NOI (Excl. RE Taxes)		\$182,660
Cap Rate	7.25%	
Add: Effective Tax Rate	<u>2.06%</u>	
Loaded Cap Rate		9.31%
Indicated Value		<u>\$1,960,931</u>
Less: FF&E (Real Estate only)		-\$50,000
Concluded Value of the Real Estate (rounded)		\$1,910,000

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Allocation of Real Estate Value

Case Study: Sales Comparison Approach

Sales Approach is best used as a “frame of reference”.

- Selecting Sale Comps
 - Apartments
 - Age-restricted apartments
- Adjustments are Subjective/Difficult to Quantify
 - Size adjustment
 - Functional obsolescence
- Units of Comparison
 - Price per Unit
 - Price per Sq. Ft. of GBA

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Allocation of Real Estate Value

Cost Approach

- Does the construction cost equal real estate value?

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Allocation of Real Estate Value

Cost Approach

- Feasibility Rent: Are rents high enough to support new construction?

	<u>Total</u>	<u>\$/Unit</u>
Replacement Cost New	\$5,966,900	\$145,534
<u>Cap Rate (Real Estate)</u>	<u>7.25%</u>	<u>7.25%</u>
NOI (real estate)	\$432,600	\$10,551
<u>Expense Ratio</u>	<u>58.98%</u>	<u>58.98%</u>
EGI	\$1,054,563	\$25,721
<u>Vacancy Rate</u>	<u>5.00%</u>	<u>5.00%</u>
PGI	\$1,110,067	\$27,075
NRA	<u>23,297</u>	
Feasible Rent (\$/SF)	\$3.97	\$2,256

- Cost does not always equal value

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Allocation of Real Estate Value

Cost Approach

- Why the construction cost may not equal RE value
- ALF are designed for providing care to senior residents?
 - Super adequate amenities:
 - Multiple elevators
 - Commercial kitchen
 - Abundant amenities
 - Nurse stations and various offices
 - Inefficiencies:
 - no kitchens,
 - 300 to 400 sf. units,
 - shared bathrooms,
 - lack of parking

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Allocation of Real Estate Value

Cost Approach: Allocation Example

Line		Ind. Living
1	Going Concern via Income	\$149.70
2	Replacement Cost New/SF	\$86.92
3	<u>Plus Land</u>	<u>\$25.00</u> <u>28.8%</u>
4	Total Cost	\$111.92
5	Average Effective Age	15 ¹
6	Depreciation	30.00% 50
7	Market Value of Land & Improvements	\$85.84
8	Implied BPP Market Value	\$63.82
9	Percentage to BPP	42.6%
10	Percentage Real Estate	57.4%

Source: Valuation of Real Estate Within Senior Living Facilities, Senior Housing & Care Journal V19.1, 2011.

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Allocation of Real Estate Value

Allocation: Final Thoughts

- What would a buyer pay for the property without the business income?
 - What kind of income could the real estate generate without a business?
 - The building was designed for AL and the delivery of services. This is an ALLOCATION of value based on the existing design.
 - This is NOT a change in the Highest and Best Use

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Allocation of Real Estate Value

Take Away Points

- Think Apartments
- Focus on Rents
- Understand the operating business, it will help with allocation

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Questions?

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