

Austin American-Statesman

SUNDAY, MAY 16, 1999

www.austin360.com

\$1.50 ★★ NS *

Tax appraisals skewed, office owners say

market value for all of Austin's office buildings.

The ultimate victims, say property owners, are the tenants who end up paying for rising property taxes through higher rents — more than 33 percent since 1995.

Some believe this trend could harm the area's economic development efforts, pricing Austin "right out of the market."

"If rent goes up because of taxes, you rethink whether you expand in Austin or San Antonio or Portland," said Phil Capron, a partner

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Appraisals of some buildings have increased more than 50 percent this year. Higher appraisals mean higher taxes.

Art Cory, chief appraiser for the Travis Central Appraisal District, uses actual sales prices and estimates of building income to determine appraised value.

But sales prices can tell a misleading story, say Austin commercial property owners who are expected to protest their appraisal increases in record numbers this year. They say Cory has misused a few sky-high sales — resulting from a short-lived feeding frenzy by REITs — to exaggerate the

comparable sales; income approach, based on a property's profits, or cost approach, based on actual construction cost less any wear and tear. The cost approach is rarely used for office buildings.

One problem with the market approach to valuing top-of-the-line office buildings is that, unlike homes, only a handful might sell in any year.

Real estate trusts' role
Nobody denies that the value of Austin real estate has risen significantly since the bust of the 1980s. With strong job growth and a healthy economy, office buildings have filled up, enabling landlords to raise rents. Since 1989, the area's occupancy rates have risen from 70 percent — among the lowest in the nation — to a tight 93.7 percent.

Enter the REITs, which combine money from many investors, much like mutual funds, to acquire new properties. And now, returns on their money forcing the REITs to be more conservative

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■ Boosted by top-dollar building purchases, high values could be damper to region's growth

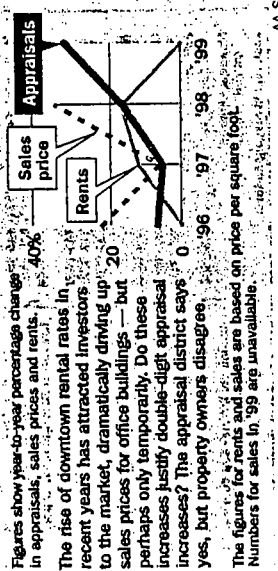
was one of several real estate investment trusts, or REITs, clamoring for office buildings. And with billions of dollars of Wall Street capital to invest, they were paying higher and higher prices to get them.

Acquisitions of prime office properties such as Bridgepoint Square, Austin Centre and Cielo Centre by REITs fueled double-digit jumps in the appraised value of office buildings in 1998 — from the city's core to the suburbs.

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Source: Colliers Oxford Commercial Research Services

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Figures show year-to-year percentage change in appraisals, sales prices and rents. The rise of downtown rental rates in recent years has attracted investors to the market, dramatically driving up sales prices for office buildings — but perhaps only temporarily. Do these increases justify double-digit appraisal increases? The appraisal district says yes, but property owners disagree. The figures for rents and sales are based on price per square foot. Numbers for sales in '99 are unavailable.

'90s office shopping spree drives appraisals

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of The SynerMark Companies, which owns 2 million square feet of commercial real estate in Austin's suburban markets. "You rethink whether you hire those five employees. I think it could have a huge reverberatory economic effect."

For Mayor Kirk Watson and supporters of the city's Smart Growth policy of encouraging downtown growth, the appraisals bring both validation and trepidation. Rising values mean a vital downtown. They also mean higher tax bills and one more reason for tenants to look elsewhere when their leases expire.

"It is at least one symbol that we are having success in trying to create a vital downtown," Watson said. "But we can't bask in that success. Instead, we need to evaluate the situation and calibrate." What sort of calibrations? Watson isn't ready to list specifics. But, knowing that downtown is more expensive for businesses, Watson said the key is to continue to make those higher taxes, slightly higher rents and parking

costs worth it to the chief executive officers and local managers who make decisions about where to lease office space.

The county appraiser stands by his numbers and has little patience for the REITs' aspendthrifts argument.

"I can't sit here and say why someone is paying that for something," Cory said. "But I can examine the sales data. If the REITs are establishing the market, that's just the way it is."

Property owners were singing a different tune about appraisal methods in the late 1980s, at the bottom of the real estate bust when the federal Resolution Trust Corp. was selling foreclosed downtown properties for what Cory's office thought were artificially low prices. At that time, the district set appraisals somewhat higher, eliciting walls from the property owners that actual RTC sales prices should be used.

"They made just the opposite argument back in the late 1980s," Cory said.

Then or now, the building owners want lower appraisals — and taxes — regardless of what the market is doing, and tax appraisers are bound by law to calculate values at market prices.

Appraisal protests are nothing new. When you're dealing with multimillion-dollar buildings, property owners usually disagree with the taxing authority. But this year, the outrage has been especially vocal.

Chet Morrison, local president of Deloitte & Touche, an accounting consulting firm, said most of his clients have instructed him to file appeals. His clients include Trammell Crow Co. and Equity Office Properties Trust, which owns such downtown properties as Franklin Plaza and One American Center.

"It's the highest I've ever seen this year," Morrison said. "My perception is that the values proposed are in excess of true market value."

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Higher office rents likely after soaring appraisals

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in their spending habits. Highgate Holdings sold Austin Centre in January 1998 for \$97 million to Crescent Real Estate Equities, a Dallas-based REIT. Highgate bought the building in 1996 for \$62.7 million. But Tom Stacy, Highgate's local partner and president of T. Stacy and Associates, said he doubts Austin Centre could have sold for that price with the current credit crunch.

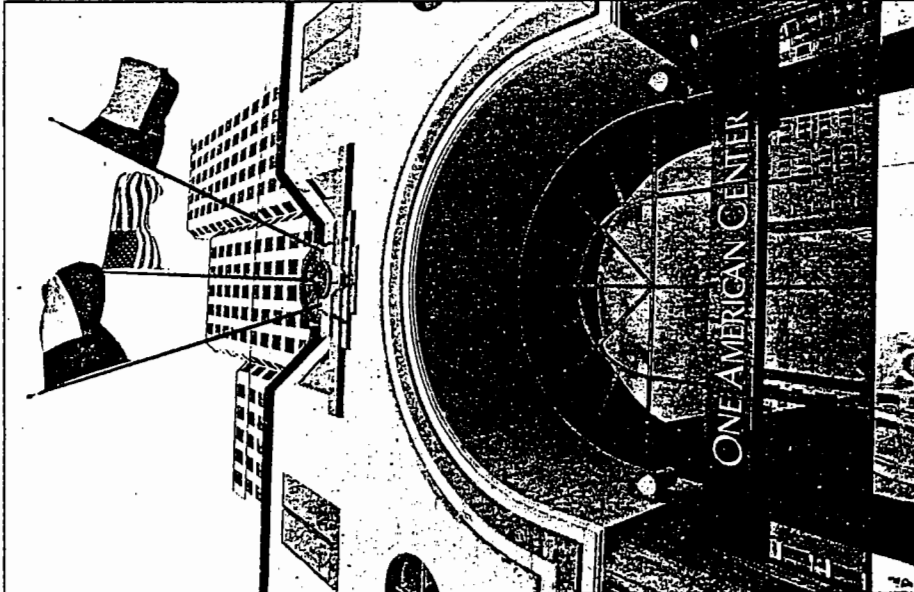
"Even if Austin Centre did represent the market at the time, there have been changes that have affected the market," Stacy said. "And even if it could sell for the same amount, it doesn't mean every building downtown is worth the same price per square foot. There are a lot of factors for an appraiser to take into account."

But the sale of Austin Centre was used to determine 1999 appraisals for the highest-quality office buildings downtown. And that has frustrated both property owners and downtown advocates who fear rising taxes will dampen the hard-fought renaissance of the city's core. Additional expenses for tenants, they fear, will send people scurrying back to the suburbs.

As the economy rebounded in the mid-1990s, the suburban office market became hot while downtown lagged. But construction couldn't keep pace with demand; suburban office space became tight and rents soared, forcing many companies to look downtown. The office towers began to fill up.

Although downtown may have been a last resort for some companies, employees realized there are advantages to the central location. Dozens of restaurants and stores are within walking distance.

But now, the rising rents could make downtown less attractive. The appraisal increase downtown would cost tenants roughly \$1 a square foot. Including costs for taxes, insurance and other direct expenses, downtown tenants typically pay between \$24 and \$32 a square foot. Most office leases allow the landlord to pass on tax increases directly to tenants.



Ralph Barrera/AA-S. The appraised value of One American Center, in downtown Austin at West Sixth Street and Congress Avenue, went from \$63,560,000 in 1998 to \$86,000,000 this year, a 35.3 percent increase.

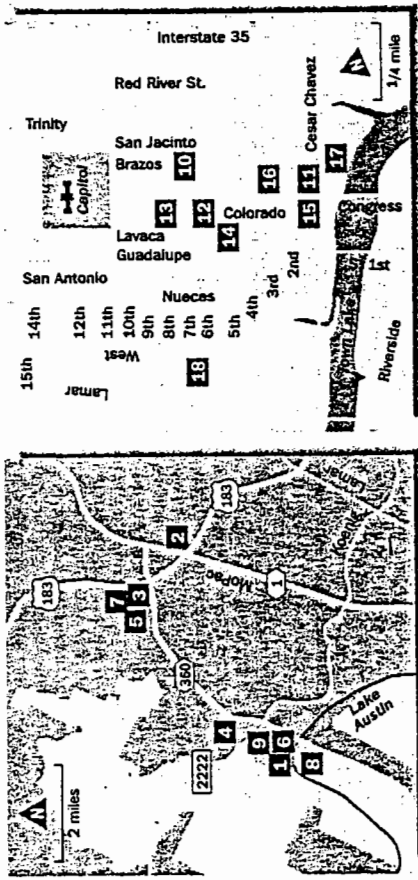
For a small business, renting perhaps half a floor or about 10,000 square feet, that extra \$10,000 a year could be a significant chunk of profit. And even for a huge law firm such as Vinson & Elkins, which uses four floors of One American Center, an additional \$80,000 to \$100,000 a year would be noticeable. That's potentially at least one less lawyer on staff, or two or three support workers.

Rising costs downtown, even before these appraisal increases, had a lot of smaller tenants heading for the hills, according to Rollee Roesner, president of Sixth River Architects. Roesner and his 15 employees in August will be leaving the 3,000 square feet in Frost Bank Plaza that they have occupied since 1994.

Back then, Frost Bank was about 60 percent empty, and his total rent was about \$14 a square foot. It's up to \$18 now and would

Urban vs. suburban

Despite this year's dramatic appraisals for downtown's largest buildings, the appraised values for the suburbs' top office buildings are still higher. Here's a look at the top nine downtown and top nine suburban office buildings.



Suburban buildings	Square footage	1998 appraisal	1999 appraisal	Percent increase, '98 to '99	1999 appraisal per square foot
1. Bridgepoint Square	406,047	\$74,000,000	\$79,000,000	6.8	\$194.56
2. 8308 MoPac	276,950	\$31,274,000	\$45,700,000	46.1	\$166.01
3. Arboretum Plaza I, II	244,585	\$34,250,000	\$41,750,000	21.9	\$170.70
4. Lakewood at the Park	216,681	\$6,583,960*	\$42,000,000	N/A	\$193.83
5. Continuum Bldg.	187,385	\$24,000,000	\$31,750,000	32.3	\$169.44
6. Bridgepoint Plaza	178,606	\$21,500,000	\$30,200,000	40.5	\$169.09
7. Arboretum Point	154,350	\$20,000,000	\$25,500,000	27.5	\$166.21
8. Plaza on the Lake I	119,995	\$14,725,000	\$23,400,000	58.9	\$195.00
9. Shepherd Mtn. Plaza	102,186	\$13,350,000	\$18,500,000	38.6	\$181.04
Downtown buildings					
10. Austin Centre	617,044	\$73,000,000	\$86,000,000	17.8	\$139.37**
11. Franklin Plaza	534,191	\$49,225,000	\$73,000,000	48.3	\$136.66
12. One American Center	519,668	\$63,560,000	\$86,000,000	35.3	\$165.49
13. Frost Bank Plaza	509,664	\$40,010,000	\$65,340,000	63.3	\$128.20
14. Bank One Tower	451,150	\$40,500,000	\$64,000,000	58.0	\$141.96
15. 100 Congress	441,332	\$46,900,000	\$70,000,000	49.3	\$158.61
16. 301 Congress	436,855	\$44,500,000	\$73,000,000	64.0	\$167.10
17. San Jacinto Center	433,044	\$47,000,000	\$65,500,000	39.4	\$151.25
18. GSP&M Building	135,409	\$9,430,129*	\$22,875,000	N/A	\$166.93

* Buildings did not exist or were under construction in 1998. ** Average for hotel and office sections. Appraisal district appraised Austin Centre office space at \$155.10 a square foot and hotel rooms at \$83.217 a room.

Sources: Travis Central Appraisal District, Commercial Broker's Network

Jay Carr/AA-S

have gone to \$26 a square foot or even higher if he renewed his lease. He also pays \$81 a month for each employee's parking in five garages downtown, except for a couple of employees who park at the Palmer Auditorium and take the "Dillo."

Sixth River is moving to Spyglass Point on MoPac Boulevard (Loop 1), just south of Zilker Park. The lease will be \$24 a square foot. Parking will be free and plentiful.

But Roesner has mixed feelings. "You lose something by going to the suburbs," he said. "You have to want to be downtown."

Some downtown advocates last week suggested that Cory should perhaps accept independent appraisals from so-called MAIs, which stands for Member of the Appraisal Institute. The idea is that these experts would produce unbiased, more-balanced appraisals.

Cory doesn't buy it. "There's also a belief that MAI stands for Made As Instructed," Cory said. "I guarantee, you put 10 MAIs in the room and you'll get 10 different values. Sure, we'll look at them. But I do not roll over and accept someone's appraisals that they went out and hired to be done for them."

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