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UNITED STATES BANKRUPTCY COURT
IN AND FOR THE DISTRICT OF ARIZONA

AVONDALE GATEWAY CENTER)
ENTITLEMENT, L.L.C.,)
Debtor.)

Chapter 11 proceedings
Case No. 2:09-bk-12153-CGC
UNDER ADVISEMENT DECISION
RE HEARING ON VALUATION
OF PROPERTY

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I. Background & Facts

The issue presented is the value of the Debtor's property in Avondale, Arizona. The determination of value is relevant both in the context of the lender's pending motion for stay relief and the confirmation of Debtor's plan.

The property consists of approximately 110 acres of undeveloped land adjacent to Interstate 10 between 107th Avenue and 115th Avenue near the "gateway" to the Town of Avondale ("Property"). It is encumbered by a first lien in the approximate amount of \$25,000,000 in favor of National Bank of Arizona ("Bank") and a second lien in the approximate amount of \$18,000,000 in favor of another lender.

The seeds of the current situation were sown in the land value boom that came to a screeching halt in 2007. The Property is reflective of that heady time. Debtor's predecessor purchased the Property for about \$5 a square foot; Debtor bought the Property in two transactions, one for \$8 per square foot in and the other for \$8.66 per square foot in late 2006. Either of the current appraisals (\$3.15 and \$1.50) represents a huge drop (60% to 80%) from the average purchase price.

Two appraisers testified at the hearing. On behalf of the Bank, Jay Lefevers offered an opinion of \$3.15 per square foot, or a total of \$15,130,000. On behalf of the Debtor, Dan Paulus offered an opinion of \$1.50 per square foot, or a total of \$7,200,000. This wide variation derives primarily from the status of the current market for undeveloped land in greater Maricopa County.

1 Both appraisers agreed that the sales comparison approach was the only appraisal approach
2 applicable to the valuation of the Property. Both agreed that the current market for raw land is
3 very thin, to the point of being non-existent. Thus, each appraiser faced the critical and difficult
4 issue of how to determine comparable sales (the primary basis for the sales comparison
5 approach) in a market where no such sales exist.

6 Lefevers' approach was to identify comparable sales from 2007 and early 2008 and then
7 struggle to derive an appropriate method to adjust the values indicated by those sales to the
8 present time. Paulus' approach was to rely upon data (including two listings and one note sale)
9 from the current market even if the properties and transactions were not actually comparable.

10 Both approaches are problematic because neither is based on actual raw land sales in the current
11 market. At the same time, given that no such sales exist, each approach reflects the best effort of
12 a valuation expert to deal with a close to impossible situation. On balance, the Court concludes
13 that Paulus' approach is more inherently reliable and will be adopted by the Court.

14 **II. Analysis**

15 *A. Lefevers.*

16 Lefevers chose four sales from 2006 and 2007. There is no serious challenge by the
17 Debtor to the comparability of these sales from the point of view of property attributes (raw land,
18 zoning, etc.) or to the minor adjustments made for location, size, etc. The essence of Debtor's
19 challenge is that the sales are not comparable because they occurred in a market that has since
20 disappeared and that the methodology used by Lefevers to adjust the sales to today's market is
21 fatally flawed. What is that methodology? First, Lefevers relied upon a national study on rental
22 rates for income producing properties and capitalization rates (with a focus on data for the west
23 valley submarket) and determined that, on average, a combination of decrease in rental rates and
24 increase in capitalization rates justified a conclusion that values were stable in 2007 and
25 decreased at the rate of .5% per month in 2008 and 3.0% per month in 2009. Then, Lefevers
26 applied those rates of decline in income producing properties to the subject raw land and
27 concluded that the four comps had decreased in the amount of 33%, 33%, 32% and 29%

1 respectively. He further testified that these rates of decline were consistent with his discussions
2 with brokers and his many years of experience.

3 Lefevers acknowledged that a more reliable method for discounting would have been to
4 find paired sales (two sales of the same property in 2007 and 2009) but accurately pointed out
5 that no such sales existed. What was troubling, however, was the contrast of his explicit refusal
6 to consider current sales data on income producing properties—rejecting such information as not
7 pertinent – while at the same time expressly relying on similar information to determine the rate
8 of decline from the high market two years ago to the lower market today. His explanation on
9 this point was unconvincing. He stated that he relied on the studies because they had excellent
10 data and some relevance in determining raw land values similarly to the land residual technique.
11 But, the bottom line is that this is data relating to a different type of property and there was no
12 credible foundation given for why such data would be useful in this context but data based on
13 current sales of the same type of land would not be pertinent.

14 In addition, the percentage decreases are not consistent with other anecdotal evidence
15 presented. For example, Paulus testified that the Bank’s chief appraiser had stated two days
16 before the trial that raw land values were down as much as 70% to 80%; while there was
17 additional testimony (though not from the chief appraiser himself) that these comments were
18 intended to be limited to certain specified types of property, the fact remains that 29% to 33% is
19 materially outside this range. Further, as noted above, the Property was acquired between
20 December 2006 and March 2007 at an approximate price of \$8.40 per acre. Lefevers’
21 comparables date from July 2007 to August 2008; his testimony was that 2007 was “flat” so no
22 downward adjustment was made to the comparable sales. Yet, compared to the subject, the
23 comparable sales suggest a drop of more than 50% (\$8.40 to \$4.30 and lower) in that general
24 time frame *even before* adjustments for the more dramatic declines of late 2008 and into 2009.
25 Even assuming that the Property was purchased at the very top of the market, the 29% to 33%
26 proposed adjustments simply don’t comport with reality suggested by the rest of the record.

27 For these reasons, the Court will not accept the analysis suggested by Mr. Lefevers.
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1 *B. Paulus*

2 As noted above, Paulus took an approach that is the mirror image of Lefever's; he relied
3 on current data other than sales of raw land, thereby raising issues as to their comparability but
4 eliminating any issue of having to estimate just how precipitous the fall in values had been since
5 2007. The difficulty of this approach is obvious; if you don't start from sales of comparable
6 property, it is difficult to derive meaningful information from the data. This problem was further
7 compounded by the fact that Paulus relied upon only one actual sale of property; his other three
8 "comps" included two listings and one "note sale." Notwithstanding these defects, the Court
9 finds that the approach is inherently more credible than Lefevres' for several reasons.

10 First, the note sale involved an obligation secured by raw land; thus, even though the
11 asset sold was not raw land, the underlying collateral was. The Bank argues that such data is
12 unreliable because it relates to a "liquidation" sale by a financial institution, not a market
13 transaction between property buyer and seller. But the reality is that the market is distressed and
14 is largely driven by financial institutions "liquidating" their collateral, whether land itself or
15 obligations secured by land. The market is not an abstract concept; it is what it is – and today, it
16 is a function of soured loans and collateral recovery. Thus, a current note sale is considerably
17 more indicative of value than an actual sale from a bygone era.

18 Second, although listings are not as reliable as actual sales, they can be relevant because
19 they relate to the same type of property as the Property. Here, Paulus substantially discounted
20 the listed amounts to reflect the normal price adjustments in such circumstances. No serious
21 challenge was raised by the Bank to the sufficiency of the discounts.

22 Finally, although the actual sale relied upon by Paulus consisted of improved lots (rather
23 than raw, unimproved land), its proximity in time allows for adjustments that are based more on
24 data than on guesswork. Thus, though not the same type of land, it is sufficiently comparable to
25 be relevant to the determination of value in this case.

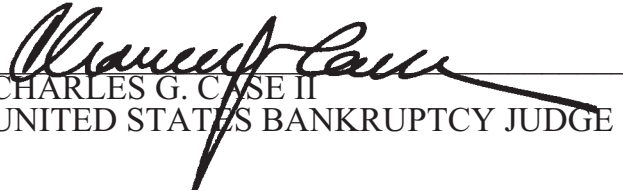
26 **III. Conclusion**

27 In short, both appraisers were faced with the difficult task of determining value in the
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1 absence of meaningful comparable sales and each tried to overcome those obstacles in different
2 ways. The Court concludes that the path taken by Paulus is materially more credible and
3 therefore adopts his proposed value of \$7,200,000.

4 Counsel for Debtor is to submit a proposed form of order.

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6 **DATED:** November 5, 2009

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9 CHARLES G. CASE II
10 UNITED STATES BANKRUPTCY JUDGE

11 Copy of the foregoing sent via facsimile and/or mailed to:

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