COMMONWEALTH OF MASSACHUSETTS

APPELLATE TAX BOARD

THE WILLOWS AT WESTBOROUGH v. THE BOARD OF ASSESSORS OF THE TOWN OF WESTBOROUGH

Docket Nos.: F252006 (FY 1999)
F256211 (FY 2000)
F259233 (FY 2001)

Promulgated:
October 16, 2002

These are appeals under the formal procedure pursuant to G.L. c. 59, §§ 64 and 65 from the refusal of the appellee to abate real estate taxes assessed under G.L. c. 59, § 38 for fiscal years 1999, 2000, and 2001.

Commissioner Egan heard these appeals. Chairman Burns and Commissioners Scharaffa, Gorton, and Rose joined her in all three decisions for the appellee.

These findings of fact and report are made on the Board's own motion pursuant to G.L. c. 58A, § 13 and 831 CMR 1.32, and are promulgated contemporaneously with the Board's decisions in these appeals.

Mark J. Witkin, Esq. for the appellant.

John M. Lynch, Esq. and *Stephen W. DeCourcey,* Esq. for the appellee.

FINDINGS OF FACT AND REPORT

On January 1, 1998, 1999, and 2000, the appellant, The Willows at Westborough, was the assessed owner of a parcel of land in Westborough located at the intersection of Lyman and East Main (Route 30) Streets, approximately a half-mile from Route 9 and two miles from the Route 9 interchange with Interstate 495. At all relevant times, the parcel contained 6.64 acres of land improved with a primarily four-story, irregularly shaped, steel frame and concrete building. The subject property is part of a continuing care community, which is operated on a 13.57-acre site and provides a continuum of senior housing and care options ranging from congregate housing, in the form of independent living and assisted living, to skilled nursing care.[1]

The subject property is located in a residential zoning district where hospitals, sanitariums, convalescent, nursing or rest homes and congregate housing are allowed by special permit. The surrounding area is a mix of commercial and residential properties with a large strip mall/shopping center located across Lyman Street. The existing uses on the subject property are authorized uses

[1] As defined by the appellant's expert on the senior housing industry, a nursing home is more like a hospital providing limited medical care and geriatric services, while a congregate care facility offers a combination of healthcare and hospitality-like services, but third parties administer medical care.

under the zoning bylaws subject to receiving a special permit. The property also appears to conform to all dimensional requirements for congregate housing.

The subject property is generally referred to as "The Willows," and it contains 172 Independent Living Units ("ILUs") and 30 Assisted Living Units ("ALUs") along with various support services.[2] The 30 ALUs within The Willows are also referred to as "Whitney Suites." The continuing care community not only includes the subject property but an additional 60-unit assisted living building, called "Whitney Place," and a rehabilitation and skilled nursing center, called "The Beaumont." Enclosed passageways interconnect the three buildings within this complex. These buildings also share several common area features such as parking, driveway access, and landscaping. The facilities are otherwise independent with respect to mechanical, electrical, and plumbing systems, as well as administrative and dining services and healthcare amenities.

For fiscal year 1999, the Assessors of Westborough ("the assessors") valued the subject property at $14,878,500 and assessed a tax thereon, at the rate of

[2] Several years before the assessment dates at issue, one of the units was converted to a doctor's office and examining room.

$15.62 per thousand, in the amount of 232,402.17. For fiscal year 2000, the Assessors valued the property at $15,085,900 and assessed a tax thereon, at the rate of $15.12 per thousand, in the amount of $228,098.80. For fiscal year 2001, the Assessors valued the property at $15,182,200 and assessed a tax thereon, at the rate of $14.03 per thousand, in the amount of $213,006.27. The appellant paid the tax for each of these fiscal years without incurring interest.

The appellant timely filed applications for abatement ("AAs") with the Assessors for the three fiscal years at issue and seasonably appealed the Assessors' denials of its abatement requests to the Appellate Tax Board ("Board"). A summary of the essential jurisdictional information is contained in the table below. On this basis, the Board found that it had jurisdiction over these appeals.

Docket Number / **Event**	**F252006 FY 1999**	**F256211 FY 2000**	**F259233 FY 2001**
Last Day for Filing AAs	02/01/1999	02/01/2000	02/01/2001
AAs Filed	01/28/1999	02/01/2000	01/29/2001
AAs Denied	02/09/1999	02/07/2000	02/16/2001
Petitions Filed with Board	05/10/1999[3]	05/08/2000[3]	04/20/2001

[3] The petitions for fiscal years 1999 and 2000 were filed with the Board on Monday, May 10, 1999 and Monday, May 8, 2000, respectively. During these two fiscal years, G.L. c. 59, §§ 64 and 65 required petitions to be filed with the Board no later than three months after their denial. In both these appeals the petitions were filed one day beyond this three-month jurisdictional requirement. Nevertheless, the Board found that the appellant had timely filed these petitions because, under G.L. c. 4, § 9, a filing period that ends on a Sunday is extended by operation of law until the next business day, which in both of these appeals was the Monday when the petitions were filed.

The subject building was built in 1987 and contains a total gross floor area of approximately 216,518 square feet. The building consists of four four-story wings extending off a two-story central core. The first floor of the central core is located off the main entrance and is known as "The Village Area." This section includes a main lobby with a reception area and staff offices, a library, a large community room with a stage, a bank, a beauty salon/barbershop, a general store, a fitness room, a crafts shop, and other small activity rooms. The second floor of the central core includes the main kitchen and dining area, which opens to an outdoor terrace at the rear of the building. A café/snack bar and a laundry area are also located here. Two centrally located passenger elevators and one freight elevator service the property. There are other small common area lounge/card rooms throughout The Willows for the use of the residents. The building is heated by gas, and portions are centrally air-conditioned. Individual units have their own air conditioners.

Of the 172 ILUs in The Willows, there are 134 one-bedroom units, 33 two-bedroom units, and 4 two-bedroom deluxe units. One unit is used as an on-site physician's or medical office. Of the 30 ALUs in The Willows, 25 are

studios and 5 are one-bedroom units. These ALUs could also be used as ILUs, depending upon demand. The Massachusetts Department of Elder Affairs has certified the Willows for up to 35 ALUs.

Each of the one- and two-bedroom units includes a fully equipped galley kitchen with double tray stainless steel sink, refrigerator, four-burner electric range and hood, Formica counters, pine cabinets and drawer cases plus disposals and, in some units, dishwashers. The one-bedroom and two-bedroom units include one or two three-fixture bathrooms, respectively, ample walk-in closet space, and stacked washers and dryers. The one-bedroom units range in size from 728 to 1,091 square feet; the two-bedroom units range in size from 1,058 to 1,136 square feet. The ILUs contain several different floor plans and may include balconies, bay windows, and dens.

The studios also include a three-fixture bathroom but only a small kitchenette consisting of Formica cabinets and counter top, refrigerator, single white porcelain sink and small-four burner electric range. They range in size from 330 to 377 square feet.

Resident rooms are decorated in neutral colors and include valences and draperies. Furniture is the resident’s responsibility. Bathrooms have step in showers

with molded seats and grab bars. The bathroom and kitchen floors are linoleum. All units are equipped with emergency call buttons.

While the building and units are well maintained and, in virtually all respects, in good to excellent condition, there is a lack of storage space for the independent units. Additionally, the HVAC system is inefficient causing poor air circulation, and none of the units contain microwaves and many lack dishwashers.

In addition to the building, the subject site contains paved and lined parking spaces, as well as paved driveway access with a circular drive at the main entrance. There are numerous foundation plantings and mulched gardens around the building and lighted walkways with adjacent lawn, benches, and plantings throughout the complex. There is also a concrete patio and a gazebo. Similar to the building, the grounds are well maintained.

The occupancy costs for the residents of the ILUs include a monthly service fee plus a one-time entrance fee that is 90% refundable (without any interest accruing) upon the earlier of re-occupancy or one year after the unit is vacated. The appellant retains the remaining 10% of the entrance fee. According to the appellant's pricing schedules, as of the first two assessment dates, entrance

fees for ILUs ranged between $110,000 to $263,000. By the third assessment date, the entrance-fee range increased to $110,000 to $269,000. The monthly service fees for the ILUs ranged from $1,439.50 to $1,931.50 for the first two assessment dates and increased to $1,510 to $2,013 by the third assessment date.

There are also additional entrance fees and monthly service fees for second occupants of ILUs. During all three fiscal years at issue in these appeals, the entrance fees were increased by $7,500 for a second occupant. The monthly service fees were increased by $738.50 as of the first two assessment dates and $757.00 for the third.

In certain situations, individuals who are unable to pay part of or even all of the entrance fees may still occupy ILUs by paying what appears to be a proportionately higher monthly service fee up to an extra $1,000 per month. As of the assessment dates in these appeals, six residents of ILUs paid either no or a reduced entrance fee along with a higher monthly service fee.

Services provided for the ILU residents include one meal per day, weekly housekeeping, flat linen service, daily local transportation, 24-hour staff and emergency response, weekly wellness clinic, thrice weekly blood pressure clinic, full-time resident recreation and

entertainment coordinator, full-time registered nurse, complete unit maintenance, and all utilities except telephone and cable.

Generally, the occupants of the ALUs pay a monthly service fee only, which varies according to the level of services provided. The Independent Plus Plan (Plan A) offers a base-level of services and amenities that include three meals per day plus snacks, routine health and wellness assessments, 24-hour supervision by certified nursing assistants, safety checks and occasional reminders, a full complement of activities, participation in the personalized exercise program, weekly housekeeping, linen service, and utilities. As of the first two assessment dates, the service fees for this plan ranged from $2,590 to $3,690 for single occupants and an additional $1,495 to $2,145 for second residents. As of the third assessment date, the range of monthly fees increased to $2,670 to $3,800 for single occupants and an additional $1,540 to $2,210 for second persons. The Catered Plan (Plan B) includes all the services provided under Plan A plus an hour per day of personal care[4] and self-administered medication management. As of the first two assessment

[4] Personal care includes assistance with showers, whirlpool baths, and occasionally, activities of daily living and managed incontinence.

dates, the service fee for this plan ranged from $3,340 to $4,440 for single occupants and an additional $2,245 to $2,895 for second persons. As of the third assessment date, the range of monthly service fees under this plan increased to $3,420 to $4,550 for single occupants and an additional $2,290 to $2,960 for second persons. The Assisted Plan (Plan C) includes the same services provided under Plans A and B plus two hours per day of personal care and daily housekeeping services. As of the first two assessment dates, the monthly service fee for this plan ranged from $3,940 to $4,995 for single occupants and an additional $2,845 to $3,495 for second persons. As of the third assessment date, monthly service fees ranged from $4,020 to $5,105 for single occupants and an additional $2,890 to $3,560 for second persons.

As of the first two assessment dates, several occupants of ALUs paid an entrance fee of up to $100,000 in exchange for a reduction in monthly service fees of $50.00 per $1,000 paid in entrance fee. As of the third assessment date, seven occupants of ALUs were paying reduced monthly fees in exchange for their entrance fee.

The appellant presented its case in chief through the testimony and reports of two expert witnesses, Christos Kuliopulos, a consultant to the senior housing industry,

and Robert L. Coleman, a licensed real estate appraiser. The assessors defended the assessed values that they placed on the subject property for the fiscal years at issue through the testimony and report of their licensed real estate appraiser, Emmet T. Logue, and the subpoenaed rebuttal testimony of Gregory J. Walsh, a real estate development consultant to the senior housing industry. The hearing officer took a view of the subject property prior to the hearing.

Mr. Kuliopulos offered a report in which he analyzed the income-producing potential of The Willows, including Whitney Suites. In his testimony and report, Mr. Kuliopulos compared the subject property's facilities and pricing structure to those of competitors in an area that included Shrewsbury, Marlborough, Worcester, and Framingham. He observed that these other area facilities were newer, better designed, and more functional than the subject property, and most of them offered more suitable amenities for senior residents. Compared to these properties, Mr. Kuliopulos considered The Willows' rate structures to be "aggressive."

Mr. Kuliopulos also evaluated the revenue and expenses associated with The Willows. For revenue, he considered four categories of income including monthly service fees,

the non-refundable portion of the entrance fees, ancillary income, and interest income and late charges. Relying primarily on The Willows' actual income, but considering competitors' charges, as well as input from The Willows' marketing director, he estimated the relevant market's monthly service fees for The Willows as of the relevant assessment dates. The following table summarizes his findings in this regard.

	Type of Unit	As of 01/01/1998	As of 01/01/1999	As of 01/01/2000
ALUs:	Studio/One-Bedroom	$2,840	$3,039	$3,026
ILUs:	One-Bedroom	$1,440	$1,440	$1,468
	Two-Bedroom	$1,732	$1,732	$1,762
	Deluxe Two-Bedroom	$1,927	$1,927	$1,962

Using these figures, Mr. Kuliopulos then projected the yearly residents' service revenue. He included income from a sub-category termed respite care, which he based on historical data. Mr. Kuliopulos described the revenue derived from respite care as income from the short-term rental of temporarily vacant units to non-residents in need of temporary housing. His projections are summarized in the following table.

	As of 01/01/1998	As of 01/01/1999	As of 01/01/2000
ALUs: 30 Studio Units	$1,022,400	$1,094,040	$1,089,360
ILUs: 134 One-Bedroom Units	$2,315,520	$2,315,520	$2,360,544
33 Two-Bedroom Units	$ 685,872	$ 685,872	$ 697,752
4 Two-Bedroom Deluxe Units	$ 92,496	$ 92,496	$ 94,176
Second Person Fee	$ 190,860	$ 146,796	$ 164,796
Second Person Meal	$ 26,136	$ 26,028	$ 29,520
Respite Care	$ 37,875	$ 15,344	$ 4,000
TOTAL RESIDENT SERVICES REVENUE	**$4,371,159**	**$4,376,096**	**$4,440,148**

Mr. Kuliopulos relied on the actual revenues generated from ancillary services at The Willows for his projections relating to this income category. His ancillary service revenue included income from leased spaces to third-party vendors, transportation charges to residents, fees for assisted daily living services provided beyond the plans, a percentage of gross receipts from hair salon, the gross revenue from snack bar sales, a percentage of gross receipts from vending machines, fees charged to non-residents for participation in the personal exercise program, and miscellaneous income from non-recurring income items. His ancillary service revenue totals for the 01/01/1998, 01/01/1999, and 01/01/2000 assessment dates are $228,125, $274,220, and $281,797, respectively. The following table summarizes his findings in this regard.

	As of 01/01/1998	**As of 01/01/1999**	**As of 01/01/2000**
Rent	$ 10,829	$ 11,276	$ 11,998
Transportation	$ 30,107	$ 23,758	$ 18,662
Healthcare	$ 92,964	$140,405	$154,322
Hair Salon	$ 4,092	$ 4,818	$ 5,327
Snack Bar	$ 65,030	$ 74,969	$ 76,224
Vending	$ 10,958	$ 10,344	$ 9,356
Personal Exercise Program	$ 8,989	$ 8,140	$ 5,758
Misc. Income	$ 5,156	$ 510	$ 150
TOTAL ANCILLARY INCOME	**$228,125**	**$274,220**	**$281,797**

Mr. Kuliopulos considered the 10% non-refundable portion of the entrance fees as another source of revenue

for The Willows.[5] To determine the revenue potential for the non-refundable piece of the entrance fees, he analyzed actual entrance fees at the subject property as well as competitive rates, which he then amortized over the remaining life expectancies of residents. His projections for this category of income as of the assessment dates of 01/01/1998, 01/01/1999, and 01/01/2000 are $409,084, $418,270, and $441,497, respectively.

Interest income and late charges comprised Mr. Kuliopulos' final income category. This revenue is derived from interest income generated from the working capital cash accounts and the late charges from residents who failed to timely pay their monthly fees. Based on historical results coupled with industry standards, he projected these amounts to be $50,501, $53,638, and $52,436, as of 01/01/1998, 01/01/1999, 01/01/2000, respectively.

The following table summarizes Mr. Kuliopulos' gross potential income for The Willows from all sources for the fiscal years at issue in these appeals.

[5] The 10% non-refundable portion of the entrance deposit is retained by The Willows upon the one-year anniversary of occupancy by the resident. For the first two months of occupancy, the entrance deposit is fully refundable. Thereafter, the non-refundable percentage increases by 1% for each month of occupancy until the 10% cap is reached after one year of occupancy.

	As of 01/01/1998	As of 01/01/1999	As of 01/01/2000
Resident Services Revenue	$4,371,159	$4,376,096	$4,440,148
Ancillary Revenue	$ 228,125	$ 274,220	$ 281,797
Entrance Fees	$ 409,084	$ 418,270	$ 441,497
Interest Income & Late Charges	$ 50,501	$ 53,638	$ 52,436
TOTAL GROSS POTENTIAL REVENUE	**$5,058,869**	**$5,122,224**	**$5,215,878**

In his gross potential income analysis, Mr. Kuliopulos did not treat the 90% refundable portion of the entrance fees as a source of revenue for The Willows. He explained that the developers of The Willows had used the original 90% refundable part of the entrance fees as a financing mechanism for developing the project. Because these fees were used to fund the development, Mr. Kuliopulos considered them a liability that actually increased as entrance fees increased. He did not consider it appropriate to impute interest income to The Willows for the 90% refundable portion of the entrance fee. He found no correlation between entrance fees and monthly service fees charged by The Willows.

Mr. Kuliopulos recognized that his gross potential income figures assumed 100% occupancy and full payment of all fees. To reach effective gross incomes as of each of the assessment dates, he analyzed the actual number of empty units at the end of the year, the number of days the units were actually vacant over the course of the year,

underwriting criteria assumed by investors, and industry data from senior housing publications. Relying on this information, he estimated a 6% vacancy and collection loss rate for all three of the fiscal years at issue. The following table summarizes his calculations for reaching effective gross income figures as of 01/01/1998, 01/01/1999, and 01/01/2000.

	As of 01/01/1998	**As of 01/01/1999**	**As of 01/01/2000**
Total Gross Potential Income	$5,058,869	$5,122,224	$5,215,878
Vacancy & Collection Loss	($ 303,532)	($ 307,333)	($ 312,953)
Effective Gross Income	**$4,755,337**	**$4,814,891**	**$4,902,925**

In determining operating expenses, Mr. Kuliopulos analyzed The Willows' historical expenses and industry data, interviewed The Willows' controller and other operating personnel, and discussed expense parameters with market participants of senior housing properties. His expense projections for the fiscal years at issue in these appeals are reflective of both industry standards and historical data, and are summarized in the following table.

	As of 01/01/1998	As of 01/01/1999	As of 01/01/2000
Administrative & General	$ 509,805	$ 531,552	$ 581,395
Management Fee @ 5%	$ 237,767	$ 240,745	$ 245,146
Insurance	$ 149,273	$ 152,373	$ 176,556
Marketing	$ 214,413	$ 232,775	$ 247,979
Property Expenses	$ 16,159	$ 15,171	$ 13,583
Plant Operations	$ 521,804	$ 518,393	$ 496,199
Dietary	$1,043,960	$1,137,121	$1,117,984
Laundry & Linen	$ 14,653	$ 17,139	$ 12,526
Housekeeping	$ 257,426	$ 225,696	$ 227,389
Health Services	$ 368,840	$ 366,259	$ 383,159
Resident Services	$ 43,640	$ 39,021	$ 38,481
Activities	$ 41,719	$ 37,534	$ 38,135
Personal Exercise Program	$ 44,599	$ 46,391	$ 41,813
TOTAL OPERATING EXPENSES	**$3,464,058**	**$3,560,169**	**$3,620,346**

For his reserve-for-replacement deduction, Mr. Kuliopulos relied on discussions with investors and reserve ranges reported in the 1997 through 1999 *State of Seniors Housing Guide*. He chose a reserve of $650 per unit because the subject facility is relatively old and several systems are nearing replacement. After deducting operating expenses and reserves for replacement from effective gross income, Mr. Kuliopulos projected the net operating income for The Willows as of 01/01/1998, 01/01/1999, 01/01/2000 at $1,160,629, $1,124,071, and $1,151,929, respectively. The following table summarizes his calculations.

	As of 01/01/1998	As of 01/01/1999	As of 01/01/2000
Effective Gross Income	$4,755,337	$4,814,891	$4,902,925
Operating Expenses	($3,464,058)	($3,560,169)	($3,620,346)
Reserve for Replacement	($ 130,650)	($ 130,650)	($ 130,650)
NET OPERATING INCOME	**$1,160,629**	**$1,124,071**	**$1,151,929**

In addition to evaluating the net operating income of The Willows, Mr. Kuliopulos investigated tangible and

intangible assets that he regarded as critical to the successful operation of the senior housing facility. The intangible assets that he analyzed include working capital, inventories, start-up/transition costs, and entrepreneurial profit. The tangible assets that he reviewed are the personal property and equipment present at The Willows that he considered necessary for the operations of a full-service congregate care facility. For this category, he considered items such as exercise equipment, mini-bus, office equipment, kitchen equipment, dining room furniture and equipment, arts and crafts items, woodworking shop equipment, lounge and meeting room furniture, common area furniture and moveable lighting, patio furniture, pool table, and convenience store items.

Mr. Kuliopulos explained that a working capital account at The Willows is necessary to fund operating expenses during times when revenues do not meet expenses and to pay departed residents their refundable deposits if their units are not timely reoccupied. Depending upon the circumstances, the working capital requirements in the senior housing sector generally range from $1,000 up to $10,000 per unit. Recognizing that stabilized facilities such as The Willows may require less working capital, he

considered a $1,000 per unit working capital reserve appropriate.

Mr. Kuliopolus explained that inventories include items necessary for the operational needs of the facility such as office supplies, food, cleaning supplies, paper goods, silverware, maintenance supplies, and the like. Based on his discussions with senior housing industry participants, he assumed a value for the The Willows' inventory of $50,000 or about $250 per unit.

Mr. Kuliopolus also described the need for start-up or transition costs in facilities such as The Willows. His interviews with buyers of senior housing properties revealed that these costs typically include such items as new accounting systems, due diligence costs, financial transition costs, training costs, standardization of policies and procedures, costs associated with employee turnover, and the like. Based on his discussions with operators and managers of senior living facilities, he estimated this cost for The Willows at $200 per unit, the lower end of a range that reaches $500 per unit.

In addition, Mr. Kuliopolus recognized entrepreneurial profit as a cost associated with assembling the tangible and intangible business assets necessary to conduct the business. Based on discussions with investors in senior

housing properties, who ordinarily require 5% to 10% of the effective gross income as the profit motivation necessary to attract capital and managerial talent to such a business venture, Mr. Kuliopolus considered a 5% profit figure as representative of market conditions for The Willows.[6]

Finally, Mr. Kuliopolus considered the value of the personal property at The Willows by reviewing the subject property's relevant financial statements and conversing with developers and facility operators familiar with equipment costs for senior housing who suggested a range of $4,000 to $6,500 per unit. Mr. Kuliopulos selected a mid-range figure of $5,600 as appropriate for The Willows and then deducted 50% for wear and tear. In this way, he estimated a value of $2,800 per unit for the personal property at The Willows on each of the three assessment dates at issue.

The appellant's valuation witness, Mr. Coleman considered three approaches for valuing the subject property, but determined that the income capitalization method was the most reliable one for valuing the subject property because of the nature of the business operated on the site and its income-producing characteristics. He did

[6] During re-direct examination, Mr. Kuliopulos agreed with Mr. Coleman's capitalization of this amount to determine an appropriate value for the entrepreneurial interest.

not rely on the cost approach because it fails to adequately consider the going-concern aspects of this type of property. He further ruled out the sales comparison approach because participants in the senior housing market do not rely on this form of analysis for purchase and sale decisions regarding these going concerns and because of a lack of market sales during the relevant time period and the presence of portfolio sales that render allocations difficult. Mr. Coleman found that the highest and best use for The Willows was its continued use "as a congregate housing facility with 171 [ILU]s and 30 [ALU]s in a good location on an aesthetically pleasing site with appropriate physical features and supporting parking and infrastructure."

Mr. Coleman collaborated with Mr. Kuliopulos and relied extensively on Mr. Kuliopulos' preceding analysis of The Willows' market income and expense figures for his valuation analysis of The Willows for the fiscal years at issue. Mr. Coleman also acknowledged Mr. Kuliopulos' expertise in identifying and valuing non-real estate items of the enterprise including both tangible and intangible items, which Mr. Coleman also adopted for use in his valuation of the subject property. Like Mr. Kuliopulos, Mr. Coleman did not regard the 90% refundable portion of

the entrance fees to be a source of income for The Willows. Rather, he believed that the fees represented a free business loan to the owner, which he termed "investment value" to a particular owner, under unique circumstances, which was not indicative of the market and, therefore, not includable in his income capitalization analysis.

Mr. Coleman derived his entire enterprise capitalization rates for his income capitalization methodology by analyzing current returns demanded by private and institutional investors for senior living facilities that are going concerns. He reviewed pertinent publications used by industry analysts and market participants. He further factored in market trends, the subject property's competitive characteristics, and its projected financial performance. He determined that the industry average capitalization rate varied from 10.00% to 12.00% over the relevant time period. Mr. Coleman also employed a mortgage-equity analysis and used a debt-coverage ratio with monthly compounding. After reviewing his data and the expectations of investors, he determined that pre-tax factor capitalization rates of 10.30% for January 1, 1998, 10.10% for January 1, 1999, and 10.30% for January 1, 2000 were appropriate under the circumstances.

Mr. Coleman's direct capitalization methodology initially valued The Willows as an entire enterprise before subtracting out the value of the non-assessable intangible assets and assessable personal property to achieve a value for the real property. In applying his methodology, Mr. Coleman used Mr. Kuliopulos' estimates and first calculated the net operating income of the entire enterprise before taxes. Mr. Coleman then adopted, with one exception, Mr. Kuliopulos' values for the intangible assets and added back the hypothetical tax associated with these intangible assets. This adjusted net income was then capitalized by the overall rate, plus a tax factor, that Mr. Coleman derived to reach an estimate of the value of The Willows' entire congregate housing enterprise. The values associated with the non-assessable intangible assets were next subtracted from the entire enterprise value leaving a value for the assessable real estate and personal property. To value the intangible entrepreneurial interest associated with The Willows enterprise, Mr. Coleman adopted Mr. Kuliopulos' estimate of entrepreneurial profit, at 5% of effective gross income, and then capitalized that amount by 25.00% to, in Mr. Coleman's view, more accurately reflect profit risks associated with the senior housing market. Finally, Mr. Coleman removed the value of the

assessable personal property to reach his $8,140,000, $8,030,000, and $8,160,000 estimates of the value of The Willows' real estate alone as of January 1, 1998, January 1, 1999, and January 1, 2000, respectively. Mr. Coleman considered his methodology to be essentially the same approach that the Board used in valuing real estate associated with a hotel enterprise in ***Analogic Corporation v. The Board of Assessors of the City of Peabody***, 25 Mass. App. Tax Bd. Rep. 473 (June 22, 1999). A summary of Mr. Coleman's methodology is contained in the following table.

DESCRIPTION	AMOUNT FY 1999	AMOUNT FY 2000	AMOUNT FY 2001
POTENTIAL GROSS INCOME:			
RESIDENT SERVICE REVENUE			
Assisted Living Units(30)			
Studio(25) 1-Bedroom(5) (per mo.)	$2,840	$3,039	$3,026
Potential Income	$1,022,400	$1,094,040	$1,089,360
Independent Living Units(171)			
1-Bedroom (per mo.)	$1,440	$1,440	$1,468
Potential Income-134 1-Bedroom	$2,315,520	$2,315,520	$2,360,544
2-Bedroom (per mo.)	$1,732	$1,732	$1,762
Potential Income-33 2-Bedroom	$685,872	$685,872	$697,752
2-Bedroom Deluxe (per mo.)	$1,927	$1,927	$1,962
Potential Inc.-4 2-Bedroom Deluxe	$92,496	$92,496	$94,176
Second Person Income Fees	$190,860	$146,796	$164,796
Additional Meals Income	$26,136	$26,028	$29,520
Respite Care	$37,875	$15,344	$4,000
Total Resident Services Revenue	**$4,371,159**	**$4,376,096**	**$4,440,148**
ANCILLARY REVENUE			
Rent	$10,829	$11,276	$11,998
Transportation	$30,107	$23,758	$18,662
Healthcare	$92,964	$140,405	$154,322
Hair Salon	$4,092	$4,818	$5,327
Snack Bar	$65,030	$74,969	$76,224
Vending	$10,958	$10,344	$9,356
Personal Exercise Program (PEP)	$8,989	$8,140	$5,758
Misc. Income	$5,156	$510	$150
Total Ancillary Revenue	**$228,125**	**$274,220**	**$281,797**
Sub-total	$4,599,284	$4,650,316	$4,721,945
Amortization of Non-Refundable Portion of Entrance Deposits	$409,084	$418,270	$441,497
Interest Income & Late Charges	$50,501	$53,638	$52,436
GROSS POTENTIAL INCOME	**$5,058,869**	**$5,122,224**	**$5,215,878**
LESS: Vacancy & Credit Loss Allowance @ 6.00%	$303,532	$307,333	$312,953
EFFECTIVE GROSS INCOME (EGI)	$4,755,337	$4,814,891	$4,902,925

DESCRIPTION	AMOUNT FY 1999	AMOUNT FY2000	AMOUNT FY 2001
OPERATING EXPENSES & RESERVES:			
Administration & General Expenses	$509,805	$531,552	$581,395
Management (5.00%)	$237,767	$240,745	$245,146
Insurance	$149,273	$152,373	$176,556
Marketing	$214,413	$232,775	$247,979
Property Expenses	$16,159	$15,171	$13,583
Real Estate Taxes	Factor	Factor	Factor
Plant Operations	$521,804	$518,393	$496,199
Dietary	$1,043,960	$1,137,121	$1,117,984
Laundry and Linen	$14,653	$17,139	$12,526
Housekeeping	$257,426	$225,696	$227,389
Health Services	$368,840	$366,259	$383,159
Resident Services	$43,640	$39,021	$38,481
Activities	$41,719	$37,534	$38,135
Personal Exercise Program	$44,599	$46,391	$41,813
Total Operating Expenses	**$3,464,058**	**$3,560,170**	**$3,620,345**
Reserv. for Replace. ($650/Unit)	$130,650	$130,650	$130,650
Tot. Operating Expenses & Reserves	**$3,594,708**	**$3,690,820**	**$3,750,995**
NET OPERATING INCOME BEFORE PROPERTY TAXES	**$1,160,629**	**$1,124,071**	**$1,151,930**
VALUE OF NON-ASSESSABLE INTANGIBLE ASSETS:			
Working Capital ($1,000/Unit)	$201,000	$201,000	$201,000
Inventories ($250/Unit)	$50,250	$50,250	$50,250
Start-Up/Trans. Costs ($200/Unit)	$40,200	$40,200	$40,200
Totals	**$291,450**	**$291,450**	**$291,450**
Entrepreneurial Profit (5% of EGI)	$237,767	$240,745	$245,146
Entrepreneurial Cap Rate	25.00%	25.00%	25.00%
Value of Entrepreneurial Interest	$951,067	$962,978	$980,585
Plus: Value of Non-Assessable Intangible Assets	$291,450	$291,400	$291,400
Tot. Non-Assess. Intangible Assets	**$1,242,517**	**$1,254,428**	**$1,272,035**
Tax Factor	1.5620%	1.5120%	1.4030%
Plus: Tax on Non-Assessable Items	$19,408	$18,967	$17,847
Tot. Net Operating Income Adjusted	**$1,180,037**	**$1,143,038**	**$1,169,777**
Enterprise Capitalization Rate	10.3000%	10.1000%	10.3000%
Tax Factor	1.5620%	1.5120%	1.4030%
Overall Capitalization Rate	11.8620%	11.6120%	11.7030%
MARKET VALUE OF ENTERPRISE	**$9,948,045**	**$9,843,593**	**$9,995,529**

MARKET VALUE OF ENTERPRISE	**$9,948,045**	**$9,843,593**	**$9,995,529**
Less: Value of Non-Assessable Intangible Assets	$1,242,517	$1,254,428	$1,272,035
Value of Assessable Personal & Real Property	$8,705,528	$8,589,165	$8,723,493
Less: Value of Assessable Personal Property (FF&E @ $2,800/Unit)	$562,800	$562,800	$562,800
ESTIMATED VALUE OF ASSESSABLE REAL ESTATE	**$8,142,728**	**$8,026,365**	**$8,160,693**
ROUNDED FAIR CASH VALUE	**$8,140,000**	**$8,030,000**	**$8,160,000**

Gregory Walsh, a real estate development and healthcare consultant, with considerable experience in the development of senior living facilities both nationally and in Massachusetts, testified for the assessors as a rebuttal witness. Mr. Walsh's testimony focused on the correlation between entrance fees like the ones charged by The Willows, which as previously stated are 90% refundable and 10% non-refundable, and monthly service fees at senior housing facilities like The Willows. According to Mr. Walsh, an absolute correlation exists between the amount of an entrance fee required of a resident by a facility and the amount charged as a monthly service fee whether or not the entrance fees are applied to any debt service associated with the facility. He testified that: "Where an entrance fee is paid, there is a lower monthly fee. And where an

entrance fee is not charged, there is a higher monthly charge."[7] Mr. Walsh enumerated several examples in The Willows' market area and throughout the Commonwealth where this correlation is evident. The assessors also introduced entrance fee and monthly service fee payment schedules from congregate care facilities (including one from an earlier fiscal year for the subject property), which substantiated Mr. Walsh's testimony that the amount of entrance fees charged appears directly related to the amount of monthly service fees required.

Mr. Walsh further testified that the entrance fee and monthly service fee payment model used by The Willows impacts the value of the real estate because "[t]he ability to utilize the entrance fees at no cost is effectively interest-free or cost-free capital that can be used to either pay-off the facility, in which case you own an asset outright with no debt against it, or it can be invested and yield a return."[8] Mr. Walsh stated that an owner of a senior housing facility who charges an entrance fee ordinarily would set aside approximately 10% of the 90% refundable portion of the entrance fees as a reserve for

[7] This testimony is recorded on page 27 of the transcript from the eleventh day of trial. Hereinafter, references to trial transcripts will be identified by the abbreviation "Tr." followed by the Roman numeral, which corresponds to the trial day, and the page number in the transcript where testimony is located.
[8] Tr. XI, p. 34.

the repayment to departed residents while using the remaining portion of the 90% refundable part to either pay down debt or earn interest. Based on his review of corporate bond and United States Treasury bond rates during the relevant time period, he concluded that a 6% rate of return for investment of these proceeds was appropriate. Accordingly, in this context, he considered the 90% refundable portion of the entrance fees a benefit, not a liability as Mr. Kuliopulos suggested, and a form of income to the owners of senior housing facilities that used this type of payment model.

The assessors' valuation expert, Mr. Logue, also relied on an income capitalization approach to estimate the value of The Willows for the fiscal years at issue because he considered it the most appropriate method for valuing this type of income-producing property. He excluded the cost approach for valuing The Willows because of the difficulty in not only estimating accrued physical deterioration and obsolescence but also in rendering certain land and building allocations. He considered the sales comparison approach unreliable because of the number of adjustments that would be necessary for these types of properties where they are ordinarily sold as entire business enterprises or as part of a larger portfolio sale.

Mr. Logue determined that the highest and best use for The Willows was a continuation of its present use.

In developing his income capitalization approach, Mr. Logue relied on actual income and expense figures provided by the appellant, actual income information from area competitors, and trade group information published by various senior housing organizations and the federal government. To reach his estimates of The Willows' value, Mr. Logue employed a methodology in which he subtracted operating expenses (excluding real estate taxes) from the annual effective gross revenues and then deducted reserves for replacements for short-lived realty items and FF&E (furniture, fixtures, and equipment) as well as a business enterprise/entrepreneurship return to reach his estimates of net operating income attributable to the real estate. He then capitalized the resulting net operating income using an overall rate plus a tax factor to reach his $17,600,000, $17,800,000, and $17,800,000 estimates of The Willows' value for January 1, 1998, January 1, 1999, and January 1, 2000, respectively.

To develop his estimates of the subject property's gross potential income as of the relevant assessment dates, Mr. Logue included the monthly service fees and second person fees actually charged at The Willows, which he found

consistent with the market. He also stabilized and incorporated the actual income from ancillary services, as well as revenue from the 10% non-refundable portion of the entrance fees. Unlike Mr. Kuliopulos and Mr. Coleman, Mr. Logue attributed what he determined to be a safe rate of interest income on the 90% refundable entrance fees because, in his view, they were part of the property's income stream and the appellant had virtually perpetual and unencumbered use of these deposits, which were paid for the right to use the facility and occupy one of the units. He testified that in imputing interest income on the 90% refundable portions of the entrance fees, he relied on several appraisal articles that endorsed the idea of imputing interest income on deposits related to the property being valued. He believed that this imputation was appropriate even if the deposits were constructive as opposed to the actual deposits paid by the residents to the appellant. On this basis, he considered both the non-refundable and refundable facets of the entrance fees part of The Willows' income.

Mr. Logue then used individual vacancy rates for the ILUs and ALUs and subtracted the resulting amounts from his gross potential revenue to reach his effective gross revenue. He next adjusted The Willows' actual expenses

upward to better comport with industry standards and subtracted them, along with a 5% management fee, from the effective gross revenue to reach his estimate of net operating income. Mr. Logue subtracted revenues for short-lived real estate and FF&E, as well as a 3% entrepreneurial return, to estimate the net real estate income to be capitalized.

Unlike Mr. Coleman's approach of valuing the enterprise as a whole and then subtracting out the value of the non-realty components, Mr. Logue subtracted a percentage deduction of 3% of effective gross income from the net operating income of The Willows to remove what he considered to be the amount of income attributable to the business portion of The Willows. Mr. Logue recognized that while there are several other acceptable ways to extract business income or value from a going concern, his technique is one of these acceptable methods. He testified that his overall deduction for the business portion of The Willows included all business components that other methods might deduct individually from income or collectively or individually from value. He considered his approach equivalent to the others.

Mr. Logue reviewed sales of senior living facilities, industry capitalization rates, and hotel and apartment

industry capitalization rates in determining that 9.5% was the most appropriate capitalization rate, for all three fiscal years at issue, to apply to the net real estate income to estimate the value of the real estate associated with The Willows.

A summary of Mr. Logue's income capitalization methodology is contained in the following table.

DESCRIPTION	AMOUNT FY 1999	AMOUNT FY 2000	AMOUNT FY 2001
Income			
Independent Living Units (172 units)	$ 3,089,274	$ 3,089,274	$ 3,089,274
Assisted Living Units (30 units)	$ 1,057,908	$ 1,057,908	$ 1,057,908
Second Person Fees	$ 186,102	$ 186,102	$ 186,102
Total Monthly Fees Income (202 units)	**$ 4,333,284**	**$ 4,333,284**	**$ 4,333,284**
Ancillary Services	$ 274,000	$ 282,000	$ 291,000
Non-Refundable Entrance Fees	$ 300,000	$ 300,000	$ 300,000
Interest Income on Entry Fees ($21,627,990 @ 5.75%)	$ 1,243,609	$ 1,243,609	$ 1,243,609
Gross Potential Revenue	**$ 6,150,893**	**$ 6,158,893**	**$ 6,167,893**
Less Vacancy:			
Independent Living (8%, 5%, & 3%)	$ 262,030	$ 163,769	$ 98,261
Assisted Living (15%)	$ 158,686	$ 158,686	$ 158,686
Total Vacancy	**$ 420,716**	**$ 322,455**	**$ 256,947**
Effective Gross Revenue (EGR)	**$ 5,730,177**	**$ 5,836,438**	**$ 5,910,946**
Operating Expenses			
Administration and General	$ 707,000	$ 728,000	$ 750,000
Insurance	$ 174,000	$ 179,000	$ 184,000
Dietary	$ 808,000	$ 832,000	$ 857,000
Marketing/Advertising	$ 171,000	$ 176,000	$ 181,000
Repairs & Maintenance	$ 358,000	$ 369,000	$ 380,000
Utilities	$ 260,000	$ 247,000	$ 247,000
Housekeeping	$ 225,000	$ 232,000	$ 239,000
Laundry & Linen	$ 15,000	$ 15,500	$ 16,000
Health & Resident Services	$ 490,000	$ 505,000	$ 520,000
Management Fee (5%)	$ 224,328	$ 229,641	$ 233,367
Total Operating Expenses (TOE)	**$ 3,432,328**	**$ 3,513,141**	**$ 3,607,367**
Net Operating Income (EGR - TOE)	**$ 2,297,849**	**$ 2,323,297**	**$ 2,303,579**
Additional Deductions			
Reserves for Replacements:			
Short Lived Real Estate (2%)	$ 89,731	$ 91,857	$ 93,347
FF&E ($450)	$ 90,900	$ 90,900	$ 90,900
Entrepreneurship Return (3%)	$ 171,905	$ 175,093	$ 177,328
Net Real Estate Income to be Capitalized	**$ 1,945,312**	**$ 1,965,447**	**$ 1,942,004**
Capitalization Rate	9.50%	9.50%	9.50%
Tax Factor	1.562%	1.512%	1.403%
Overall Rate	11.062%	11.012%	10.903%
Indicated Fair Cash Value	**$17,585,537**	**$17,848,231**	**$17,811,648**
Rounded Fair Cash Value	**$17,600,000**	**$17,800,000**	**$17,800,000**

There are many similarities in the parties' approaches for valuing The Willows for the fiscal years at issue in these appeals. For example, both parties considered the highest and best use of The Willows to be its continued existing use. In addition, both parties' valuation experts eschewed the cost and sales-comparison approaches and instead relied on income capitalization methodologies. With the exception of one item of potential income, both parties' valuation experts considered virtually the same items and corresponding amounts of income for The Willows. With the exception of the imputed interest income on the 90% refundable portion of the entrance fees, the parties' valuation experts calculated gross potential incomes for the fiscal years at issue that are within 3% to 5% of each other. Moreover, the parties' valuation experts' total operating expenses are virtually identical, and their reserves for replacement fall between $130,000 and $184,500. Even the parties' valuation experts' capitalization rates are within one percentage point of one another for all three fiscal years at issue.[9]

Even though the parties' valuation experts use different income capitalization methodologies to estimate

[9] The Board recognizes that Mr. Logue used a capitalization rate that he considered appropriate for determining the value of the real estate while Mr. Coleman used a rate that he considered appropriate appropriate for ascertaining the value of the entire enterprise.

the value of The Willows' real estate for the fiscal years at issue,[10] the most fundamental discrepancy between the parties' valuation experts in valuing the real estate associated with The Willows for the fiscal years at issue in these appeals is their treatment of the 90% refundable portion of the entrance fees. Mr. Coleman did not factor them into his methodology at all, while Mr. Logue considered the imputed interest earned on them part of The Willows' income stream. Interestingly, if Mr. Coleman had included this disputed income in his approach, his estimates of The Willows' value as of January 1, 1998, January 1, 1999, and January 1, 2000 would be approximately $17,800,000, $17,900,000 and $17,950,000, respectively,[11] well above the corresponding assessed values and essentially equivalent to Mr. Logue's estimates of value. The following table summarizes this comparison.[12]

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[10] Mr. Coleman first values The Willows' enterprise as a whole and then subtracts values for the intangible and tangible (or non-realty) assets to reach his estimate of the subject property's real estate value, while Mr. Logue calculates the net operating income of the enterprise as a whole and then subtracts the income attributable to the intangible and tangible assets before capitalizing the remainder to reach his estimate of the subject property's real estate value.

[11] By adding Mr. Logue's calculation for the amount of interest income earned on the refundable portion of the entry deposits ($21,627,990 x 5.75% = $1,243,609) to Mr. Coleman's gross potential income figures for each of the assessment dates, and then continuing with Mr. Coleman's methodology, his estimates of value are increased to these figures.

[12] The Board also notes that if the income attributed to the business components of the enterprise in Mr. Logue's methodology is increased to a higher percentage more consonant with the values attributed to them by Mr. Coleman in his approach, the resulting adjusted values on the relevant assessment dates still support the corresponding assessments.

	As of January 1, 1998	**As of January 1, 1999**	**As of January 1, 2000**
Assessed Values	$14,878,500	15,085,900	$15,182,200
Mr. Logue's Values	$17,600,000	$17,800,000	$17,800,000
Mr. Coleman's Adj. Values	$17,800,000	$17,900,000	$17,950,000

On the basis of all of the evidence, the Board finds that, under the circumstances present in these appeals, it is appropriate to impute a reasonable rate of interest on the 90% refundable portion of the entrance fees and include that income in The Willows' income stream when valuing the property using an income capitalization approach. The Board finds that, both at The Willows and industry-wide, the amount of the monthly service fees and the amount of entrance fees are directly related to the overall amount that a senior living facility charges a resident for the right or privilege to live there. They are both components of the cost of occupancy at these facilities. The Board further finds that, in the instant appeals, the payment of the 90% refundable portion of the entrance fees to The Willows is the basis for imputed interest income to the owner. Because, however, 90% of the entrance fee is refundable to the resident within one year after leaving the facility or re-occupancy, whichever occurs sooner, the Board finds that the income that accrues to the owner is

equivalent to the value to the owner of the right to use the 90% refundable portion of the entrance deposit for the period that extends from payment to repayment. Even though the 90% refundable portion of the entrance fees may not constitute an actual deposit on the relevant assessment dates, since those funds apparently were used to pay down financing and are not now segregated into any identifiable account, the Board, like Mr. Logue, finds that these fees are tantamount to a deposit for valuation purposes and should be considered at least a constructive deposit. The Board finds that a reasonable measure of the income attributable to this deposit in any year is the amount of interest that reasonably and safely could be earned on the 90% refundable portion of the entrance fees during the fiscal year.

The appellant argues that the 90% refundable portion of the entrance fees is neither the basis for imputed interest income nor an asset, but rather a liability to The Willows that must be repaid. According to the appellant, the value of the 90% refundable portion of the entrance fee is simply reflected in the investment value of the subject property to its owner. The appellant asserts that the payment of these fees is a unique circumstance, peculiar to the owner of The Willows, which is not indicative of the

market. The appellant further contends that the initial entrance fees were used, years ago, as a financing mechanism, so there is no "fund" or "deposit" actually accruing interest. Therefore, the appellant maintains there is no income actually being generated into The Willows' revenue stream, and none should be imputed.[13] The Board finds that the appellant's conclusions regarding the 90% refundable portion of the entrance fees are misplaced in the context of these appeals.

First, the Board finds that, as Mr. Walsh testified, the 90% refundable portions of the entrance fees are a benefit to the owner not a liability in this context. The Board finds that the owner can use the fees as a financing mechanism while only retaining 10% as a reserve for repayment in any given year, or invest them all and earn interest. In either circumstance, it strains credulity to characterize the 90% refundable portions of the entrance fees as a liability for valuation purposes. To the extent that parts of the 90% refundable portions of the entrance fees may need to be repaid to departing residents from time

[13] Mr. Walsh testified that the 90% refundable portion of the entrance fees affects the value of the real estate associated with The Willows. The appellant urges a different interpretation of Mr. Walsh's testimony that suggests any income from or attributable to these refundable deposits is business income and, therefore, irrelevant to this inquiry. Even if the Board were to accept, *arguendo*, the appellant's contention in this regard, the Board would find that the income is still includable in the revenue stream of the entire enterprise in both of the valuation experts' income capitalization methodologies.

to time, new residents replenish them. During the years at issue, there was always a nearly full accrual of entrance deposits at The Willows, which is an established and stabilized facility, and at least a theoretical reserve.[14] The Board finds that the 90% refundable portions of the entrance fees are clearly a benefit to the owner of The Willows in this context, and it is entirely appropriate, indeed necessary, to impute a reasonable rate of interest on the deposits, whether they are actual or constructive, and include that amount in the revenue stream of the entire enterprise when using income capitalization methodology to estimate the value of the real estate associated with the enterprise.

Second, the Board finds that the value of the 90% refundable portions of the entrance deposits is not simply investment value to a particular owner who happens to charge them. Rather, they are part and parcel of the monthly service fees that are also charged by the facility. As Mr. Walsh testified and as the experience at The Willows itself reveals, the amount of entrance fees and monthly

[14] If the refundable entrance fees were initially considered an asset, then the inclusion of an offsetting liability probably would be appropriate. This, however, is not the appellant's argument, and even if it were, it would not change the Board's finding that a reasonable rate of interest should be imputed on the 90% refundable portions of the entrance fees and included in the income of the income capitalization methodology used to value the real estate associated with The Willows.

service fees are directly, although inversely, related because monthly service fees are higher where entrance fees are lower or non-existent and *visa versa*. The appellant, however, contends that because the monthly service fees charged by The Willows, which is an older facility with fewer amenities than its competitors, are at the high-end of the scale, there is no correlation between entrance deposits and service fees. The Board finds that to the extent The Willows is able to charge relatively high monthly service fees in conjunction with its entrance fees, it is because of the market, the success of its own marketing, and factors that render The Willows very desirable to residents, such as its location, reputation, security, service plans, and the like. As examples from the actual experience at The Willows show, without entrance fees, the monthly service fees charged by The Willows are often commensurately higher, and where ALU residents pay entrance deposits, which are not ordinarily required of them, lower monthly service fees are charged. This correlation between entrance fees and monthly service fees at The Willows demonstrates their interrelationship for valuation purposes.

Moreover, and as discussed in the assessors' brief, the 90% refundable portion of the entrance fees should not

be considered simply a free business loan or mere investment value to a particular owner, as suggested by Mr. Coleman. The evidence here amply shows that the predominant market-based model for payment for residency in these types of senior living facilities is one that includes both entrance fees and monthly service fees that correlate with one another. Accordingly, the 90% refundable portion of the entrance fee is not personal to the owner of The Willows, but rather typical of the market. Under these circumstances, any owner of The Willows, not just the present one, is entitled to use the 90% refundable entrance fees interest-free. As stated in THE APPRAISAL INSTITUTE, THE APPRAISAL OF REAL ESTATE at 26 (12th ed. 2001): "If the investor's requirements are typical of the market, investment value will be the same as market value." The Board recognizes that how an owner actually chooses to use the 90% refundable portions of the entrance fees is irrelevant to the notion that a reasonable rate of return on them constitutes income and the return is part of the revenue stream for facilities, like The Willows, that charge them. Therefore, the interest-free use of these proceeds should be reflected, through the imputation of a reasonable rate of interest income on them, in any income

capitalization methodology employed for valuing the subject property.[15]

On this basis, the Board finds that Mr. Coleman’s failure to incorporate income from the 90% refundable portion of the entrance fees was error and so significantly undermined his valuation methodology and his estimates of value as to render them unreliable and of little probative value. Moreover, by modifying Mr. Coleman’s approach to account for this imputed income in The Willows’ revenue stream, his methodology supports the assessments for all three fiscal years at issue. The Board further finds that, under the circumstances present in these appeals, Mr. Logue’s income capitalization methodology is the more appropriate one for estimating the value of the real estate associated with The Willows. Mr. Logue’s approach more closely follows the methodology previously approved by the Board in nursing home appeals. “Even if the

[15] The assessors also argued that if Mr. Coleman did not include the imputed interest earned on the 90% refundable portions of the entrance fees in the revenue stream of The Willows in his income capitalization methodology, he, at least, should have considered The Willows’ use of the deposits to retire its debt in the development of his capitalization rates where he employed a mortgage-earnings analysis. They further maintained that by failing to do so, Mr. Coleman’s application of the theory underpinning his valuation methodology was inconsistent and contradictory. If Mr. Coleman had adjusted his capitalization rate as suggested by the assessors, even without changing anything else, the resulting capitalization rates would have produced values for the real estate associated with The Willows well in excess of the assessed values for all of the fiscal years at issue in these appeals.

entrepreneurship return of 3% in Mr. Logue’s approach is adjusted upward to more closely correspond to Mr. Coleman’s entrepreneurial profit of 5% (plus his other intangibles, which the Board rejects under the circumstances present in these appeals), the resulting real estate values derived from Mr. Logue’s adjusted approach still support the assessments for all three fiscal years at issues.” Finally, Mr. Coleman attempted to justify his methodology by stating that it was comparable to the one used by the Board in valuing the real estate associated with a hotel enterprise in ***Analogic Corporation***, *supra*. However, unlike the appellant here, the owner of the hotel at issue in ***Analogic Corporation*** built that facility to the specifications of the franchisee that then operated it. The owner was contractually obligated to incur certain additional business expenditures on behalf of the franchisee. The methodology that the Board used in ***Analogic Corporation*** was specific to and based on the evidence in those hotel appeals. The senior congregate housing at The Willows is part of a continuing care facility and is more similar to a health care facility or nursing home than a hotel. Mr. Coleman did not demonstrate the appropriateness of using the ***Analogic Corporation*** valuation approach in the instant appeals or adequately

explain why he departed from the Board's established methodology in valuing the entrepreneurial interest in nursing home cases. Under the circumstances, the Board finds that Mr. Logue's methodology is the more appropriate one to use in these appeals.

For these reasons, the Board finds that the appellant has failed to carry its burden of proving that the assessors overvalued The Willows for the fiscal years at issue. Therefore, the Board decided these appeals for the assessors.

OPINION

The principal issue in these appeals is whether the subject real estate was overvalued in fiscal years 1999, 2000, and 2001.[16] To make that determination, the Board found that interest income should be imputed on the 90% refundable portion of the entrance fees associated with The Willows during the fiscal years at issue and included in the income aggregation of the income capitalization methodology used in estimating the value of the real estate associated with the subject property. The Board further

[16] Recently, the Board addressed the issue of the exemption of congregate care facilities from local real estate taxation. ***Western Mass. Lifecare Corp. v. Assessors of Springfield,*** 25 Mass. App. Tax Bd. Rep. 658 (1999), *aff'd,* 434 Mass. 96 (2001). The valuation issue presented in these appeals, however, is a matter of first impression.

found that the assessors' valuation expert's income capitalization methodology was the more appropriate one to use under the circumstances present in these appeals. The Board relied upon the following principles in deciding these appeals for the assessors.

The assessors are required to assess real estate at its fair cash value. G.L. c. 59, § 38. Fair cash value is defined as the price on which a willing seller and a willing buyer will agree if both of them are fully informed and under no compulsion. ***Boston Gas Co. v. Assessors of Boston***, 334 Mass. 549, 566 (1956). Accordingly, fair cash value means its fair market value. ***Id.***

"Prior to valuing the subject property, its highest and best use must be ascertained, which has been defined as the use for which the property would bring the most." ***Tennessee Gas Pipeline Co. v. Assessors of Agawam,*** 26 Mass. App. Tax Bd. Rep. 226, 234 (citing ***Conness v. Commonwealth,*** 184 Mass. 541, 542-43 (1903)); ***Irving Saunders Trust v. Assessors of Boston,*** 26 Mass. App. Ct. 838, 843 (1989) and the cases cited therein. A property's highest and best use must be legally permissible, physically possible, financially feasible, and maximally productive. APPRAISAL INSTITUTE, THE APPRAISAL OF REAL ESTATE at 305-308 (12th ed., 2001). *See also* ***Skyline Homes, Inc. v. Commonwealth,***

362 Mass. 684, 87 (1972); ***DiBaise v. Town of Rowley,*** 33 Mass. App. Ct. 928 (1992). In determining the property's highest and best use, consideration should be given to the purpose for which the property is adapted. APPRAISAL INSTITUTE, THE APPRAISAL OF REAL ESTATE at 315-16; ***Tennessee Gas Pipeline Co.,*** *supra* at 235. In the present appeals, both parties' valuation experts and this Board found that the continuation of the subject property's existing use as a senior congregate housing facility, which is part of a senior continuing care community providing a continuum of senior housing and care options, constituted its highest and best use. Accordingly, the Board rules that the subject property's highest and best use is its continued existing use.

Generally, real estate valuation experts, the Massachusetts courts, and this Board rely upon three approaches to determine the fair cash value of property: income capitalization, sales comparison, and cost reproductions. *See* ***Correia v. New Bedford Redevelopment Authority***, 375 Mass. 360, 362 (1978). "The board is not required to adopt any particular method of valuation," ***Pepsi-Cola Bottling Co. v. Assessors of Boston***, 397 Mass. 447, 449 (1986), but the income capitalization method "is frequently applied with respect to income-producing

property." ***Taunton Redev. Assocs. v. Assessors of Taunton***, 393 Mass. 293, 295 (1984). Use of the income capitalization method is appropriate when reliable market sales data are not available. ***Assessors of Weymouth v. Tammy Brook Co.***, 368 Mass. 810, 811 (1975); ***Assessors of Lynnfield v. New England Oyster House***, 362 Mass. 696, 701-702 (1972); ***Assessors of Quincy v. Boston Consolidated Gas Co.***, 309 Mass. 60, 67 (1941). "[T]he introduction of evidence concerning value based on [cost] computations has been limited to special situations in which data cannot be reliably computed under the other two methods." ***Correria,*** 375 Mass. at 362.

The income capitalization method is also appropriate for valuing real estate improved with a continuing care facility, such as a nursing home. *See, e.g.,* ***Northampton Nursing Home, Inc. v. Assessors of Northampton,*** 383 Mass. 884, 885 (1981); ***Axelrod v. Assessors of Boxborough***, 1 Mass. App. Tax Bd. Rep. 183, 185 (1982), *aff'd,* 392 Mass. 460 (1984); and ***Guidrey v. Assessors of Wayland,*** 22 Mass. App. Tax Bd. Rep. 129, 133 (1997). Both parties' valuation experts used income capitalization methodology to estimate the value of the real estate associated with The Willows for the fiscal years at issue. The Board finds and rules that income capitalization methodology is the most

appropriate approach for estimating the value of the real estate associated with The Willows for the fiscal years at issue. Under the income capitalization approach, valuation is determined by dividing net operating income by a capitalization rate. *See* ***Assessors of Brookline v. Buehler***, 396 Mass. 520, 522-523 (1986). Net operating income is obtained by subtracting expenses from gross income. ***Id.*** at 523. For nursing homes, net income to be capitalized is obtained by further subtracting reserves for short-lived real estate and personal property (or FF&E) and entrepreneurship return, thereby excluding the income attributable to the tangible and intangible assets associated with the entire enterprise from the income attributable to the real estate. *See* ***Guidrey,*** *supra* at 132-34.

Under the circumstances present in these appeals, the Board finds and rules that the income capitalization methodology used to value the real estate associated with The Willows should include in its income analysis a reasonable imputation of interest on the 90% refundable portion of the entrance fees. *Cf.* ***Linus Oakes, Inc. fka Parkway Medical Buildings, Inc. v. Department of Revenue and Douglas County Assessors,*** 15 OTR 186, 2000 Ore. Tax LEXIS 16 (2000)(sanctioning the imputation and inclusion in

income capitalization methodology for valuing the real estate associated with a congregate care facility of interest income on refundable entrance fees that are assumed to be quasi-trust funds and are paid in addition to monthly service fees by residents entering the facility).[17] Because the appellant's valuation expert, Mr. Coleman, did not include this income in his analysis, his methodology is fatally flawed. The Board noted that when it included the missing revenue in his methodology, the resulting estimates of value supported the assessments.

Moreover, the Board finds and rules that Mr. Logue's income capitalization approach is the more appropriate one to use in these appeals. It is consistent with the methodology used and approved in analogous nursing-home appeals before this Board. *See, e.g.,* ***Guidrey****, supra.* The Board further finds and rules that even if the business component in Mr. Logue's approach (entrepreneurship return) is increased to more closely correspond to the value attributed to the intangible business assets by Mr. Coleman, or to more closely approximate the entrepreneurship return in service-intensive nursing-home-valuation appeals like ***Guidrey***, the resulting real estate

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[17] Interestingly, the valuation expert in the Oregon case imputed a mortgage interest rate of 9% on the refundable entrance fees on the premise that owners of these facilities ordinarily use the deposits to finance or pay-down financing on the project. ***Id.*** at *15.

values derived from Mr. Logue's adjusted approach still support the assessments for all three fiscal years at issue. In addition, the Board finds and rules that Mr. Coleman did not demonstrate the appropriateness of using his methodology gleaned from ***Analogic Corporation v. Assessors of Peabody,*** 25 Mass. App. Tax Bd. Rep. 473 (1999), in these appeals or adequately explain why he departed from the Board's methodology in valuing the entrepreneurial interest. Accordingly, the Board finds and rules that the appellant failed to meet its burden in proving that the subject property was overvalued for the fiscal years at issue.

The mere qualification of a person as an expert does not endow his testimony with any magic qualities. ***Boston Gas Co. v. Assessors of Boston,*** 334 Mass. at 579. "The board [is] not required to believe the testimony of any particular witness but it [can] accept such portions of the evidence as appear to have the more convincing weight. The market value of the property [can] not be proved with mathematical certainty and must ultimately rest in the realm of opinion, estimate, and judgment . . . (citations omitted). The board [can] select the various elements of value as shown by the record and from them form . . . its own independent judgment." ***Assessors of Quincy v. Boston***

Consolidated Gas Co., 309 Mass. at 72. *See also* ***North American Philips Lighting Corp. v. Assessors of Lynn***, 392 Mass. 296, 300 (1984); ***New Boston Garden Corp. v. Assessors of Boston***, 383 Mass. 456, 473 (1981); ***Jordan Marsh Co. v. Assessors of Malden***, 359 Mass. 106, 110 (1971). In these appeals, the Board is persuaded from a consideration of all of the evidence that imputed interest on the 90% refundable portion of the entrance fees is income to The Willows and should be included as such in any income capitalization methodology that attempts to value the real estate associated with it.

In making its determination of fair cash value, the Board may take its view of the premises into account. ***Westport v. Bristol County Commissioners***, 246 Mass. 556, 563 (1923); ***Avco Manufacturing Corp. v. Assessors of Wilmington,*** 12 Mass. App. Tax Bd. Rep. 132, 143 (1990); ***Arthur D. Little, Inc. v. Assessors of Cambridge***, 2 Mass. App. Tax Bd. Rep. 22, 28 (1982).

The burden of proof is upon the appellant to make out its right as a matter of law to an abatement of the tax. ***Schlaiker v. Assessors of Great Barrington***, 365 Mass. 243, 245 (1974). "By holding that the assessment is entitled to a presumption of validity, we are only restating that the taxpayer bears the burden of persuasion of every material

fact necessary to prove that its property has been overvalued." ***General Electric Co. v. Assessors of Lynn***, 393 Mass. 591, 599 (1984). In appeals before this Board, a taxpayer "may present persuasive evidence of overvaluation either by exposing flaws or errors in the assessors' method of valuation, or by introducing affirmative evidence of value which undermines the assessors' valuation." ***Id.*** at 600 (quoting ***Donlon v. Assessors of Holliston,*** 389 Mass. 848, 855 (1983)).

The Board finds and rules here that, upon consideration of all of the evidence, the appellant has failed to meet its burden of proving that the property is overvalued. Therefore, the Board decides these appeals for the assessors.

The Board's Decision in these appeals is promulgated simultaneously with this Findings of Fact and Report.

APPELLATE TAX BOARD

By: ______________________________
Abigail A. Burns, Chairman

A true copy,

Attest:__________________________
Clerk of the Board