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# Distinguishing Hotel Sales from Market Value for Property Tax Purposes

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# Presenter

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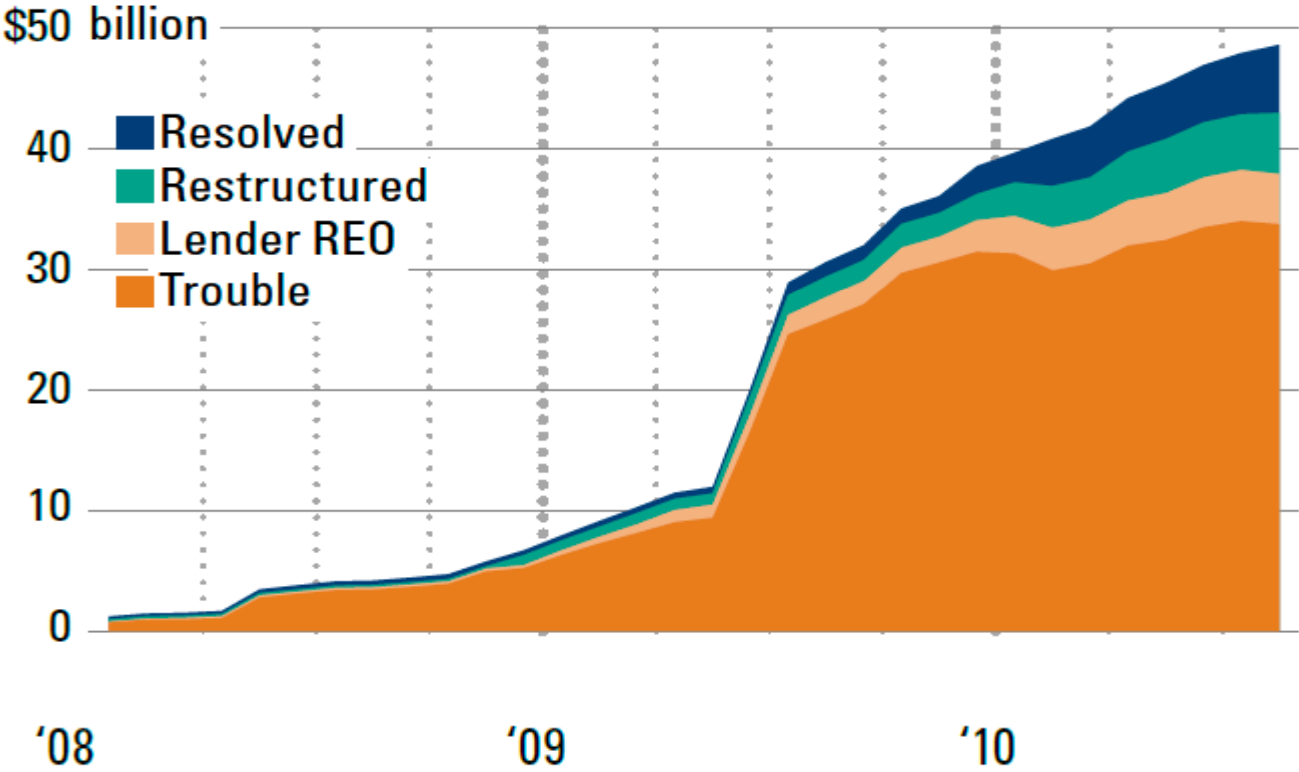
- Mark S. Hutcheson, Partner, Popp, Gray & Hutcheson, LLP
- Texas APTC Representative
- IPT CMI Designation Committee

# Market Overview

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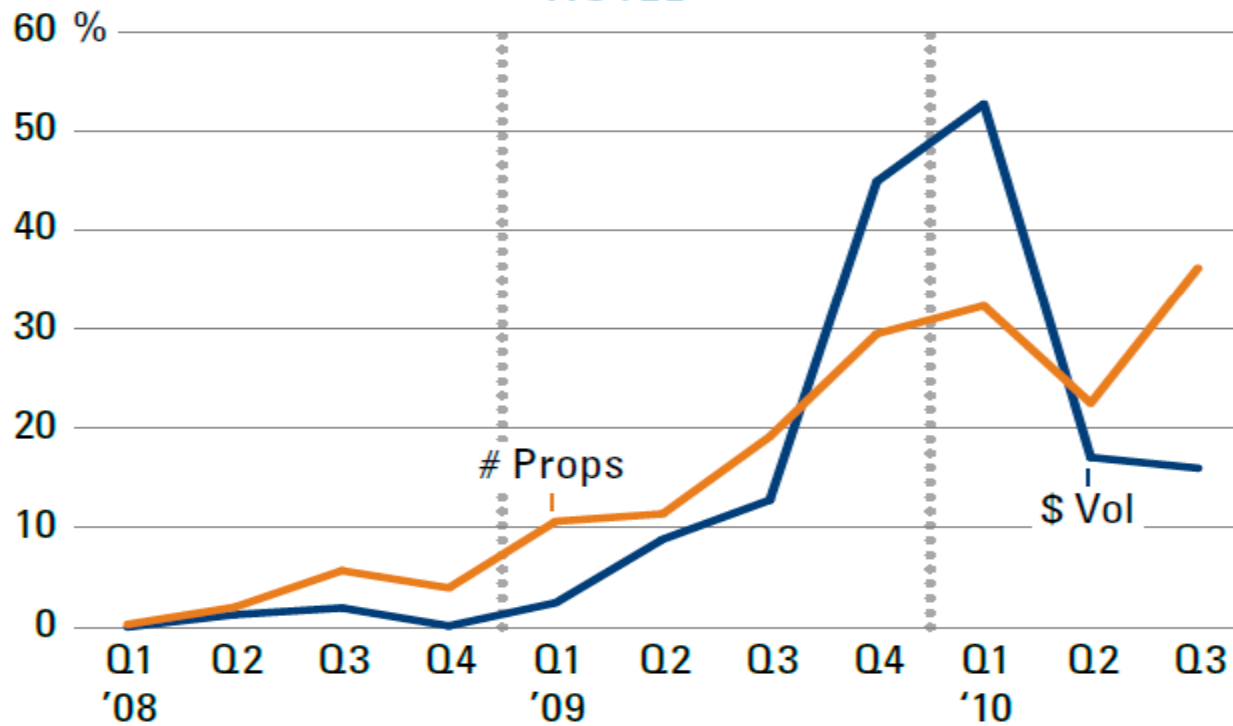
- Distressed Sales (peaked at 50% of Volume in 2010)
- Transaction Volume Coming Back
- Commercial Mortgage Maturities Will Shape Market over Next 5 Years

## CUMULATIVE DISTRESS VOLUME HOTEL



Source - Real Capital Analytics

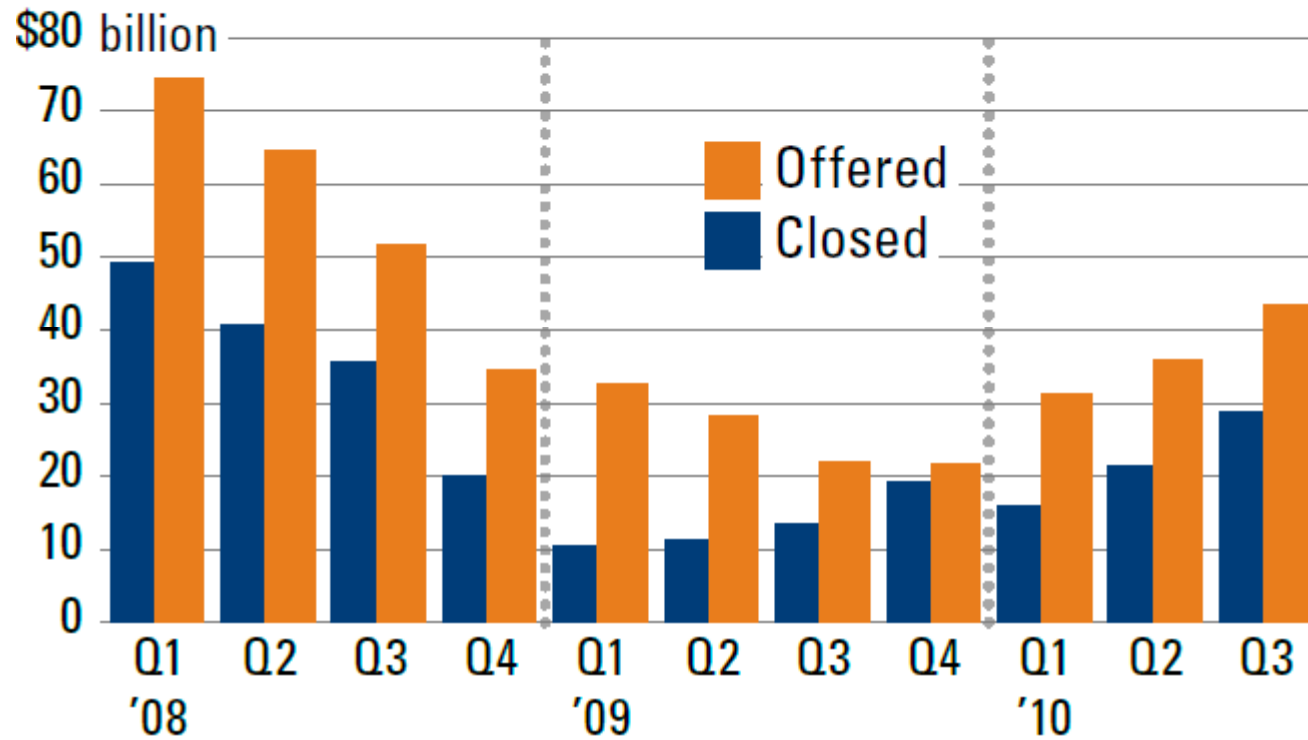
## PERCENT OF SALES ASSOCIATED WITH DISTRESS HOTEL



Source - Real Capital Analytics

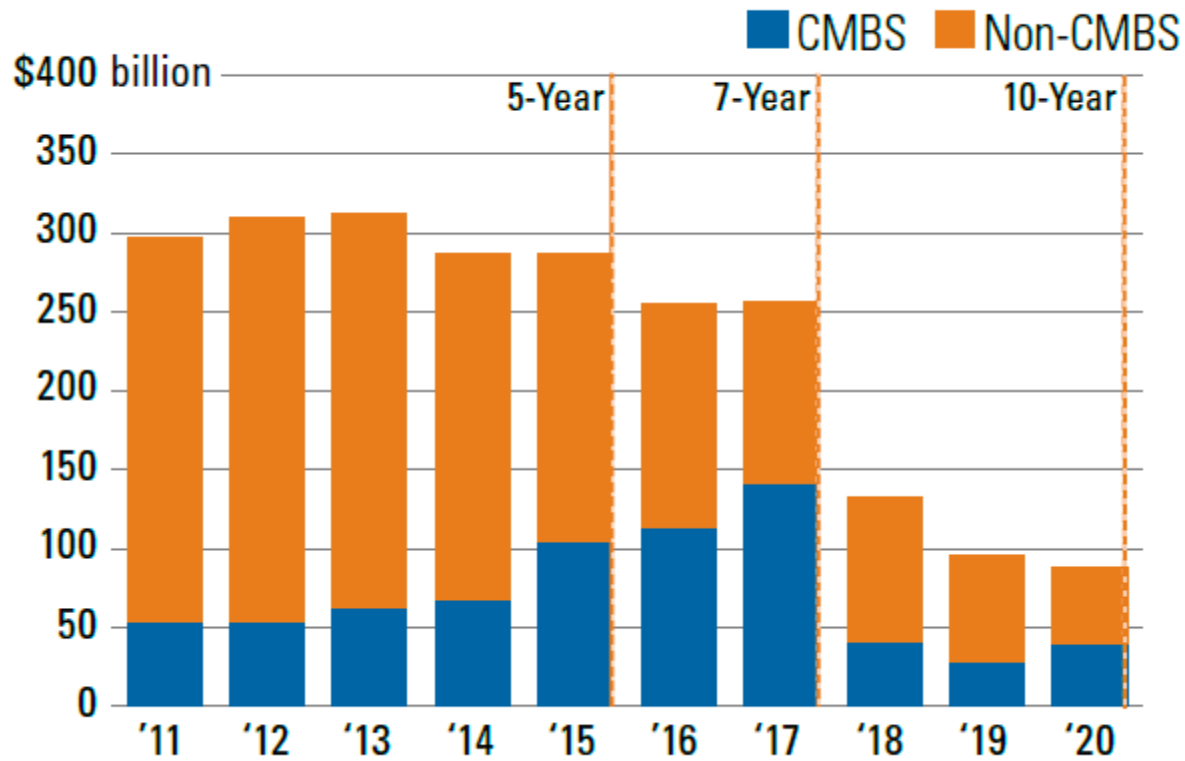
## CLOSED VS OFFERED VOLUME

ALL PROPERTY TYPES



Source - Real Capital Analytics

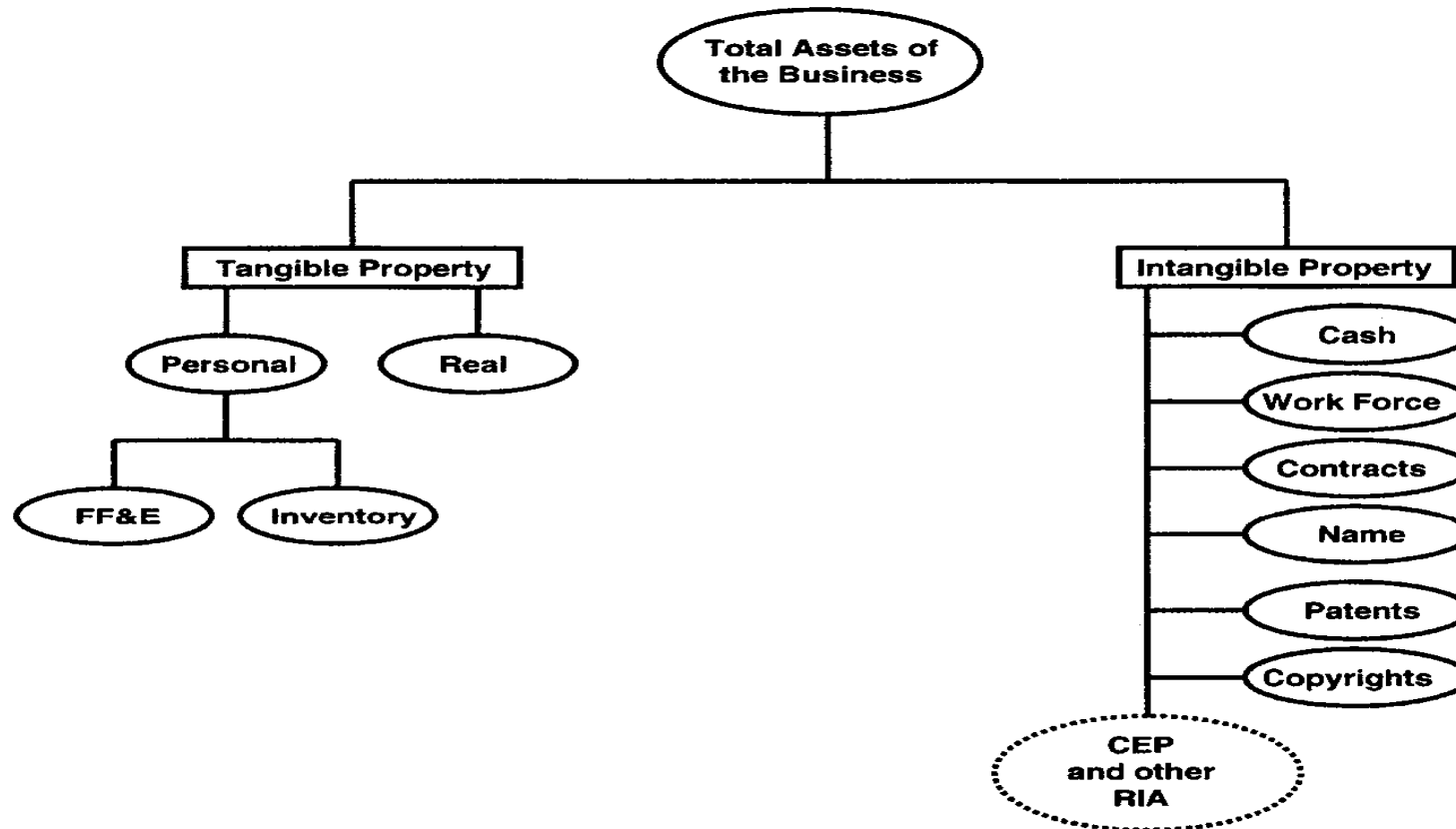
## PROJECTED COMMERCIAL MORTGAGE MATURITIES



Source: Foresight Analytics

# What's in a Sale?

## Components of a Going Concern or Business



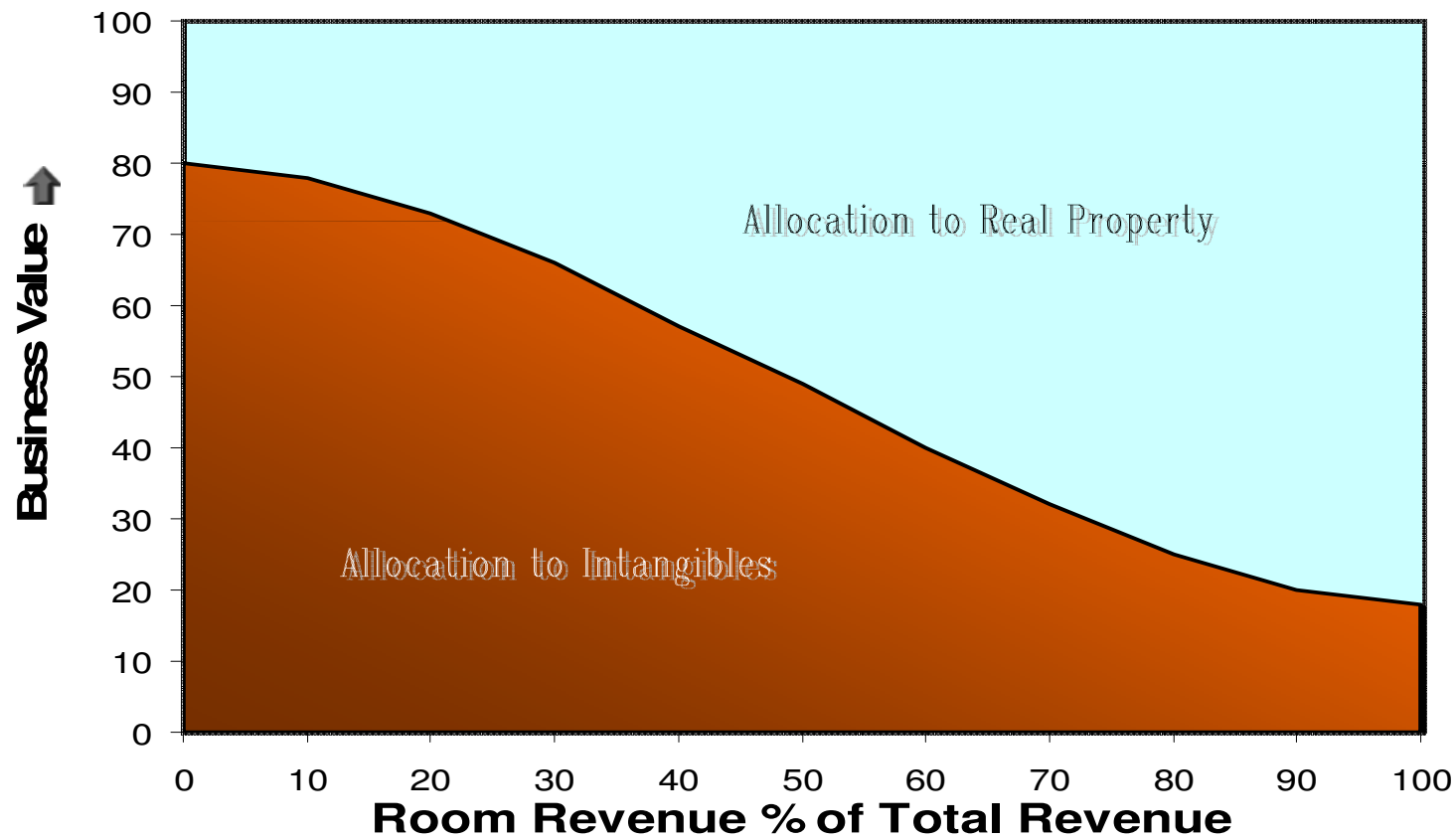


# Allocating Intangibles Among Hotel Types

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- Intangible Value Tends to Increase with Size and Complexity of Hotel Business
  - Convention
  - Historic Hotel
  - Limited Service
  - Economy/Budget

# Business Value / Room Revenue Relationship









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# Segregating Intangible Assets

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- Income Approach

Forecast Income and Expense

– Deduct Replacement Allowance

= Net Operating Income

– Deduct Start-Up Costs

– Deduct FFE (return of and on)

– Deduct Brand Premium (STR Index)

Capitalize resulting NOI (loaded rate)

Account: 110042  
multiple  
 Tax Year: 2009

Hotel: **Marriott Plaza**  
**San Antonio**  
 Type: Full Service

Rooms: 251  
 Built: 1979

REVENUE	2009 Forecast	Per Key	Ratio
Rooms	\$ 9,116,205	\$ 36,320	70.0%
Food/Beverage	\$ 2,969,885	\$ 11,832	22.8%
Telecommunications		\$ -	0.0%
Other/Misc.	\$ 936,045	\$ 3,729	7.2%
(Total Revenue)	\$ 13,022,135	\$ 51,881	100.0%

EXPENSES	2009 Forecast	Per Key	Ratio
<b>DEPARTMENTAL</b>			
Rooms	\$ 1,707,826	\$ 6,804	19.1%
Food/Beverage	\$ 2,067,677	\$ 8,238	23.1%
Telecommunications		\$ -	0.0%
Other/Misc.	\$ 286,037	\$ 1,140	3.2%
(Total Departmental Expenses)	\$ 4,061,540	\$ 16,181	45.4%
<b>UNDISTRIBUTED</b>			
Admin/General	\$ 973,774	\$ 3,880	10.9%
Repairs/Maintenance/Utilities	\$ 1,239,448	\$ 4,938	13.9%
Marketing	\$ 819,448	\$ 3,265	9.2%
(Total Undistributed Expenses)	\$ 3,032,670	\$ 12,082	33.9%
<b>FIXED</b>			
Insurance	\$ 105,248	\$ 419	1.2%
Lease/Permit/License/Margin Tax	\$ 145,607	\$ 580	1.6%
(Total Fixed Expenses)	\$ 250,855	\$ 999	2.8%
Management Fees	2.2% \$ 289,091	\$ 1,152	3.2%
Incentive Fees / Franchise	5.0% \$ 651,107	\$ 2,594	7.3%
Reserves	5.0% \$ 651,107	\$ 2,594	7.3%
<b>TOTAL EXPENSES (W/O TAXES)</b>	<b>\$ 8,936,370</b>	<b>\$ 35,603</b>	<b>100.0%</b>
<b>NET OPERATING INCOME TO GOING CONCERN</b>	<b>\$ 4,085,765</b>	<b>\$ 16,278</b>	<b>31.4%</b>

BUSINESS VALUE DEDUCTIONS	Term	Mort Const	Per Key	Cost	Annual Return	Per Key	Ratio
Start-Up Costs	25 yrs	11.18%	\$ 16,240	\$ 4,076,240	\$ 455,724	\$ 1,816	4.5%
Annualized Return on and of FFE	8 yrs	18.01%	\$ 11,000	\$ 2,761,000	\$ 497,256	\$ 1,981	4.9%
Residual Intangibles		<b>STR Index</b>		2% \$ 260,443		\$ 1,038	2.6%
(Total Business Deductions)				\$ 1,213,422		\$ 4,834	12.0%

NET OPERATING INCOME TO REAL PROPERTY			
	\$ 2,872,343	11,444	22.1%
Capitalization Rate	10.80%		
Tax Rate	2.53%		
Loaded Overall Rate =	13.33%		

RRM	RRM	RRM
<b>VALUE TO REAL PROPERTY</b>	<b>\$ 21,556,043</b>	<b>\$ 85,881</b>
		<b>2.36</b>



# Net Lease Approach

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- Based on non-REIT hotel leases of real property
- Real property leases reviewed range from 7% to 13% of total revenue
- Cap at real estate rate or hotel rate?
- Settlements based on 15% of total revenue capped at 10% (or a 1.5 total revenue multiplier)

# Room Revenue Multiplier

PKF	Room Rev Ratio (RRR)	NOI Margin	NOI/RRR	Loaded	Going Concern (RRM)	RRM @ 60%	RRM @ 70%	RRM @ 80%	
Over 200 Rooms	64.2%	26.90%	0.41900	10.87%	3.85	2.31	2.70	3.08	
Over \$100 REVPAR	64.9%	27.80%	0.42835	10.87%	3.94	2.36	2.76	3.15	
South Central	64.7%	27.30%	0.42195	10.87%	3.88	2.33	2.72	3.11	
					<b>Average =</b>	<b>3.89</b>	<b>2.34</b>	<b>2.72</b>	<b>3.11</b>
					<b>Median =</b>	<b>3.88</b>	<b>2.33</b>	<b>2.72</b>	<b>3.11</b>

# Assessor Methodologies

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## Income Approach (Direct Cap)

- deduct management and franchise fees, and reserves (3-5%)
- capitalize NOI (using Korpacz)
- determine % of NOI attributed to business value (20-35%)
- capitalize business value income by 2x applied cap rate
- cross checks value
  - RRM
  - Sales – indicate 2.7RRM
  - \$1000 x RevPar x # of Rooms

# Assessor Methodologies

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- Income Approach (Direct Cap)
  - Utilize trailing 12 months income and expense
  - Add back the management and franchise fee
  - capitalize NOI+ (using Korpacz)
  - deduct a straight 20% off for business value

# Assessor Methodologies

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## Income Approach

- use trailing 12 months income
- deduct management and franchise fees, and reserves (3-5%)
- loads tax rate
- capitalize NOI (using Korpacz)
- deduct start-up costs (up to \$5000/key) below line
- deduct personal property assessment

# Assessor Methodologies

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- Income Approach (GRRM)
  - Real Value = 2.50 x Room Revenue for Full Service
  - Real Value = 2.25 x Room Revenue for Limited Service

# Questions

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