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SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2015-006912 04/18/2017

HONORABLE ROGER E. BRODMAN

CLERK OF THE COURT
M. Corriveau
Deputy

WELLS FARGO BANK N A WADE M BURGESON

v.

TERRENATE ENTERPRISES INC, et al. TYLER J GRIM

RULING ON MARKET VALUE AFTER EVIDENTIARY HEARING

On April 10, 2017, the Court held an evidentiary hearing pursuant to A.R.S. § 33-814(A). The Court heard testimony from Dorothy Koster, Fernando Cornejo, Albert Nava and William Dominick. The Court reviewed affidavits from Ms. Koster, Mr. Cornejo and Mr. Dominick. The Court reviewed the exhibits in this case.

The parties have a dispute over the fair market value of two separate properties. The first is called the "Pinal Property." It consists of a restaurant, a banquet facility and some office space in Casa Grande. The second is called the "Sunland Property." It consists of a restaurant in Eloy. The trustee's sale was held on May 20, 2015.

The Court believes the two properties are in different financial conditions. The Court finds that the Pinal Property was in significantly worse financial condition. There was no persuasive evidence that the Cornejos had the ability to pay rent on the Pinal Property. The Court was persuaded that the Pinal Property was "overbuilt." The Court was persuaded that, due to the mixed nature of the property, the Pinal Property presented a marketing challenge. It appears to the Court that Terrenate lost money in 2014, even without paying debt service or property taxes. Terrenate has not paid property taxes for 2013 – 2014. A successfully functioning business pays its taxes. The office space for the Pinal Property was only 46% occupied, and evidence shows that the lease was expiring in April 2015. Indeed, it appears that the Cornejo's financial problems coincide with their building the Pinal Property. In short, the Court concludes that the Pinal Property was not a profitable business.

Mr. Dominick's analysis was based on the premise that Terrenate and the Pinal Property was a successful business. He wrote that "the property owner was successfully operating a Mexican restaurant and leasing out a portion of the office building." Exhibit 57, page 6. He testified that the only reason the two restaurants shut down was because of the foreclosure. Mr. Dominick wrote:

> Based on the financial information provided by the previous owner, food and banquet sales revenues appear to be more than adequate to sustain the business, presuming typical and reasonable expenses, including real property/facilities ownership/lease structure. Thus, continued use of the property as a full-service, sit down restaurant and banquet facility is considered financially feasible.

Exhibit 57, page 41.

Yet the financial records indicate that the Pinal Property was operating at a loss, even though it failed to pay property taxes or debt service. *See* Exhibit 46.001. For the reasons stated below, and supported by the notion that the Cornejos didn't run into financial trouble until they expanded their operations, the Court finds that Mr. Dominick's assumption of a successful business at the Pinal Property was not supported by the preponderance of the evidence.

On the other hand, the Sunland Property was in financially better shape. Even though revenues were decreasing, the Sunland Property had the ability to pay rent. In contrast to the Pinal Property, the Sunland Property is appropriate for a going concern evaluation. As a result, the Court believes that a different analysis is appropriate when a fair market value is determined for each of the properties.

1. <u>Pinal Property</u>

The Pinal Property is a freestanding, sit-down restaurant totaling 8832 square feet, 2048 square feet banquet hall and a separate office building totaling 3546 square feet.

The main point of dispute between Mr. Nava and Mr. Dominick was valuation of the restaurant. Mr. Nava believes the office building has a value of $640,500, while Mr. Dominick believes it has a value of 650,000. *See* Exhibit 57 at page 68.

With the exceptions noted below, the Court found Mr. Nava persuasive in his evaluation. Mr. Nava concluded that, using the Sales Comparison approach, the fair market value of the Pinal Property was $2,545,000. Using an Income Approach, the value was $2,450,000. The estimated market value was $2,500,000. Exhibit 39, pages 70-71.

The Court was persuaded that Mr. Nava's comp analysis was more accurate than Mr. Dominick's comp analysis on the Pinal Property. Mr. Nava used vacant buildings in determining his comps; the Court was persuaded that his use of comps was more appropriate. The Court believes that vacant, owner occupied restaurants would provide the most accurate comps. The Pinal Property, although not vacant, could be treated as such. It was losing money. The owner had not paid significant property taxes. For practical purposes, it was not a successful operation. Mr. Dominick indicated that "the going concern premise revolves around the assumption that a company is expected to continue operating well into the future (usually indefinitely)." Affidavit at ¶ 17. Although this assumption may be fair for the Sunland Property, the Court does not believe it is an accurate assumption for the Pinal Property. In short, the Court adopts Mr. Nava's overall assessment of the Pinal Property over Mr. Dominick's overall assessment because the Court, among other things, rejects the notion that the Pinal Property was a successful business or that the Cornejos would have continued to run a restaurant on the property. The Court also believes that Mr. Nava's use of owner occupied, vacant restaurants provides better comps than Mr. Dominick's use of chain restaurants like a Chili's.

The Court parts ways with Mr. Nava's analysis when he deducted approximately $166,000 for lease up costs. First, Mr. Nava's report indicates that some of the brokers with whom he spoke do not believe lease up costs were a necessary deduction. *See* Exhibit 39 at page 35 ("Mr. Ruble also noted that neither an owner/user nor investor purchaser would deduct a vacancy allowance"); page 61 ("no vacancy or collection loss is deducted from the subject's gross income"). In addition, this practice appears specially designated by Wells Fargo. Having used vacant restaurant buildings in calculating comps, the Court does not believe that a deduction for lease up costs is appropriate.

The Court rejects defendants' argument that Mr. Nava's report fails to accurately capture fair market value at the time of the trustee's sale because it was completed in late March and the trustee's sale occurred 55 days later. Persuasive evidence demonstrates that there was no significant change to either the property or the market during the two months between March and May. Indeed, even Mr. Dominick used sales from a wide period of time and called the market "relatively stable." *See* Exhibit 57, page 53. The Court finds that an appraisal dated March 25, 2015 accurately reflected the value of the property on May 20, 2015.

Accordingly, the Court finds that the most accurate reflection of the fair market value of the Pinal Property is Mr. Nava's approach without correction for lease up expenses. As a result, the Pinal Property has a fair market value of $2,500,000 as of the date of the trustee's sale. *See* Exhibit 39, page 71.

2. <u>The Sunland Property</u>

The Court believes that a "going concern" evaluation is proper for the Sunland Property. The restaurant had been in operation for many years. It was successful enough through 2007 that the Cornejos wanted to expand operations. The financials for the business indicate that it was making enough in net revenues to cover rent. Although the Court would hesitate to call the Sunland restaurant "successful" (it was delinquent on property taxes), the Court believes that the Sunland restaurant satisfies the assumption that it would continue to operate well into the future.

In contrast to the Pinal Property, the Court finds Mr. Dominick's analysis more accurate than Mr. Nava's on the Sunland Property. In general, the Court finds Mr. Dominick's comps more accurate than Mr. Nama's comps. The restaurant comps used by Mr. Dominick were in business; the restaurant comps used by Mr. Nava were not. In short, the Court finds Mr. Dominick's analysis more credible because he did not assume the Sunland Property was vacant.

Using the Sales Comparison Approach, Mr. Dominick finds the value of the property to be between $540,000 and $600,000. Exhibit 58 at page 51. Using the Income Capitalization Approach, Mr. Dominick finds the value to be between $530,000 and $600,000. However, Mr. Dominick notes that the household income in the area of the comps is significantly higher than the household income in Eloy. Exhibit 58, page 49. Given the rural location and the fact that residents in the area of the property are on the lower end of the income spectrum, the Court finds that Mr. Dominick's lower range of values to be more appropriate. The Court chooses $540,000.

Accordingly, the Court finds that the most accurate reflection of the fair market value of the Sunland Property as of the date of the trustee's sale is Mr. Dominick's lower end estimate of $540,000.

3. <u>Property taxes</u>

Pursuant to A.R.S. § 33-814, the fair market value means that "prior liens and encumbrances" are deducted. The Court finds Ms. Koster credible when she testified that the unpaid real property taxes due on the Pinal Property were $148,040 as of the date of the trustee's sale. The Court also finds that the outstanding real property taxes on the Sunland Property were $16,219.84.

ORDERS

IT IS ORDERED that the fair market value of the Pinal Property as of the date of the trustee's sale was $2,500,000 minus $148,040, or $2,351,960.

IT IS FURTHER ORDERED that the fair market value of the Sunland Property as of the date of the trustee's sale was $540,000 minus $16,219.84, or $523,780.16.

IT IS FURTHER ORDERED that, within 20 days from the filed date of this order, plaintiff shall submit a form of judgment containing Rule 54(c) language consistent with the terms of this Order.