

*AN APPRAISAL OF THE
OFFICE BUILDING
LOCATED AT
1539 11th AVENUE
HELENA, MT*

*DATE OF VALUATION
DECEMBER 23, 2013*

FOR

*DEPARTMENT OF NATURAL RESOURCES & CONSERVATION
TRUST LAND MANAGEMENT DIVISION*

*BY
J. MICHAEL JOKI, MAI, SRA
HELENA, MONTANA*

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December 31, 2013

John Grimm
Department of Natural Resources & Conservation
Trust Land Management Division
P.O. Box 201601
Helena, MT 59620-1601

RE: An appraisal of the office building located at 1539 11th Avenue in Helena, MT.

Dear John:

In accordance with your contract dated September 13, 2013 I have made the necessary inspection and analysis to appraise the above referenced property. The attached report provides the essential data and detailed reasoning employed in estimating my final value estimate. The report contains 57 pages.

I have appraised the property as a whole and owned in fee simple. I assume no responsibility for matters that are legal in nature nor do I render any opinion as to title.

The property being appraised is a three story office building with a full basement that has a total square footage of 25,008 SF in the four floors. The site is 60,000 SF however this building functions on a 47,878 SF site because 12,122 SF of this site is leased to the adjoining property owner. The contributory value of the leased land is also valued in this appraisal report.

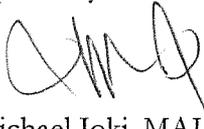
The value reported is qualified by certain definitions, assumptions and limiting conditions, and certification which is set forth within the attached report. The analysis contained herein is considered to be a summary appraisal report. This appraisal report is intended to conform with the Uniform Standards of Professional Appraisal Practice.

Based on my analysis, the market value of the subject property, as set forth, documented and qualified in the attached report under conditions prevailing on December 23, 2013 was:

SEVEN HUNDRED SEVENTY-EIGHT THOUSAND DOLLARS
\$778,000

I direct your attention to the data, discussions and conclusions which follow.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'J. Michael Joki', written in a cursive style.

J. Michael Joki, MAI, SRA
Montana State Certified
General Real Estate Appraiser #152

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INTRODUCTION

J. Michael Joki, MAI, SRA
HELENA, MONTANA

SUBJECT PROPERTY PHOTOGRAPH



The portion of the subject site that supports the office building is outlined in green, and the leased portion of the subject site is outlined in blue. These boundaries approximate.

SUMMARY OF IMPORTANT FACTS AND CONCLUSIONS

<i>PURPORTED OWNER:</i>	State of Montana.
<i>PROPERTY TYPE:</i>	Professional Office Building.
<i>LOCATION OF PROPERTY:</i>	This property is addressed 1539 11th Avenue in Helena, Montana
<i>SITE:</i>	A 60,000 SF site of which 12,122 SF is leased to the adjoining property owner. The office building and its site improvements function on 47,878 SF of land.
<i>IMPROVEMENTS:</i>	The office building has 7,352 SF in the basement and first level, and there is 6,680 SF on the second level and 3,624 SF on the third level. This totals 25,008 SF.
<i>PROPERTY RIGHTS APPRAISED:</i>	Fee Simple.
<i>ZONING:</i>	General Commercial District - B2.
<i>PRESENT USE:</i>	Professional Office Building
<i>HIGHEST AND BEST USE:</i>	Redevelopment with a new building
<i>DATE OF VALUATION:</i>	December 23, 2013
<i>SITE VALUE:</i>	\$778,000
<i>DEMOLITION COSTS:</i>	\$370,000
<i>CONCLUDED ESTIMATE OF MARKET VALUE:</i>	\$778,000

ASSUMPTIONS AND LIMITING CONDITIONS

This is to certify that the appraiser in submitting this statement and opinion of value of subject property acted in accordance with and was bound by the following principles, limiting conditions and assumptions. Unauthorized use of this report is set forth below.

1. No responsibility is assumed for matters that are legal in nature nor is any opinion rendered on title of property appraised.
2. Unless otherwise noted, the property has been appraised as though free and clear of all encumbrances.
3. Where the values of the land and the improvements are shown separately, the value of each is segregated only as an aid to better estimate the value which it lends to the whole parcel, rather than value of that particular item if it were by itself.
4. All maps, areas, plans, specifications, and other data furnished your appraiser were assumed to be correct. No survey of the property was made by this firm. Furthermore, all numerical references to linear measurements, area, volume or angular measurements should be assumed to be "more or less" (+/-) and are accurate to a degree consistent with their use for valuation purposes.
5. This appraisal considers only surface rights to the property with consideration of current zoning and land use controls. The estimate of highest and best use will form the basis for the value estimate. This appraisal does not consider mineral, gas, oil or other natural resource rights that may be inherent in the ownership of the property.
6. A copy of the report completed by ALM Consulting, LLC that is dated December 11, 2011 was provided to me. This document reports the findings from a hazardous materials inspection, and the testing and consulting for the office building that is the subject matter of this appraisal report. In this report recommendations are made for asbestos and lead based paint. As shown in this report it was found there is asbestos and lead based paint in this building however it is in good condition and can be managed in place. It is also reported that these items in their current condition do not pose a health risk. However, if this building is renovated or razed these items would have to be abated.

I have relied on this report as being accurate because I am not qualified to detect such substances. A copy of the report completed by ALM Consulting, LLC is included in the addenda. John Grimm reported to me that no updates to this report or any other reports addressing hazardous materials have been completed for the subject property.

7. The Americans with Disabilities Act (ADA) became effective January 26, 1992. I have not made a specific compliance survey and analysis of this property to determine whether or not it is in conformity with the various detailed requirements of the ADA.
8. The appraiser is not a seismologist's. This appraisal should not be relied upon as to whether a seismic problem exists, or does not actually exist on the property. The property which is the subject of this appraisal is within a geographic area where earthquakes and other seismic disturbances have previously occurred and where they may occur again. Except as specifically indicated in the report,

no seismic or geologic studies have been provided to the appraiser concerning the geologic and/or seismic condition of the property. The appraiser assumes no responsibility for the possible affect on subject property on seismic activity and/or earthquakes. We have not made a specific compliance survey and analysis of this property to determine whether or not it is in conformity with the various detailed seismic requirements by the City or County. It is possible that a survey of the property could reveal that the property does not meet the required seismic requirements. If so, this fact could have a negative effect upon the value of the property. Since we have no direct evidence relating to this issue, we did not consider possible noncompliance requirements in estimating the value of the property.

9. All data contained in this report and in the appraiser's files, as obtained from other sources, upon which to any degree the opinions and conclusions were based, are considered reliable and believed to be true and correct. However, the appraiser does not assume responsibility for the accuracy of such items that were obtained from other parties.
10. The projections of income and expense herein contained were based on information provided from the property owner as well as data extracted from the local real estate market. This information is believed to be accurate and is based on the best data available at the time this report was written. However, since projections are based on assumptions about circumstances and events that have not yet taken place, they are subject to variations that may arise as future operations actually occur. Accordingly, your appraiser cannot give assurance that the projected results will actually be obtained. Also, it should be understood that the underlying assumptions are based on present circumstances and information currently available. Because circumstances may change and unanticipated events may occur subsequent to the date of this report, the reader must evaluate the assumptions and rationale in light of the circumstances then prevailing.
11. There shall be no obligation to give testimony or attendance in court by reason of this appraisal with reference to the property in question unless arrangements have been previously made and at an additional fee.
12. Disclosure of the contents of this appraisal report is governed by the by-laws and regulations of the Appraisal Institute.

Neither all nor any part of the contents of this report especially the conclusions as to value, the identity of the appraiser, or the firm with which he is connected, or to the MAI and SRA designation, shall be disseminated to the public through advertising media, news media, public relations media, sales media, or any other public means of communication without the prior written consent of the appraiser.

13. J. Michael Joki, MAI, SRA, specifically does not authorize the out-of-context quoting from or partial reprinting of this appraisal report.
14. The liability of J. Michael Joki, MAI, SRA and employees is limited to the client and to the fee collected. Further, there is no accountability, obligations or liability to any third party. If this report is placed in the hands of anyone other than client, the client shall make such party aware of all limiting conditions and assumptions of the assignment and related discussions. The appraiser assumes no responsibility for any costs incurred to discover or correct any deficiencies of any type present in the property; physically, financially, or of a legal nature.

15. The fee for this appraisal report is for the service rendered and not for time spent on the physical report or for the physical report itself.
16. This appraisal report is prepared for the sole and exclusive use of the appraiser's client the State of Montana, Department of Natural Resources & Conservation Trust Land Management Division. No third parties are authorized to rely upon this report without the expressed written consent of the appraiser.
17. This Summary Appraisal Report is intended to comply with the reporting requirements set forth under Standard Rule 2-2(b) of the Uniform Standards of Professional Appraisal Practice for a Summary Appraisal Report. As such, it presents only summary discussions of the data, reasoning, and analysis that were used in the appraisal process to develop the appraiser's opinion of value. Supporting documentation concerning the data, reasoning and analysis is contained in the appraiser's file.. No third parties are authorized to rely upon this report without the expressed written consent of the appraiser.

DESCRIPTION, ANALYSIS AND CONCLUSIONS

J. Michael Joki, MAI, SRA
HELENA, MONTANA

SCOPE OF THE APPRAISAL

All known, available, relevant market data considered to have an impact on the market value of subject property has been considered. As identified under Assumptions and Limiting Conditions and as explained under Property Rights Appraised, the title is assumed to be free and clear of liens and encumbrances.

John Grimm, the acting Chief of the Real Estate Management Bureau for DNRC contacted me to appraise this office building. The Department of Corrections state employees were the last to occupy this building which was vacated sometime in 2010. It is my understanding the State of Montana needs a market value estimate of this property so internal decisions can be made regarding its future use.

On December 23, 2013 John Grimm met me on site and we viewed the interior and exterior of the building. John Grimm was able to answer a number of questions I had concerning this property. I completed my property inspection on December 23, 2013 and this is also the day all photographs of the subject property were taken.

The neighborhood and surrounding competitive market areas were researched to find comparable market data. Real Estate agents, property owners, property managers and real estate appraisers in Helena were interviewed during this process. This market data has been confirmed by personal contact with the buyer, seller, broker, or property manager. All of the comparable land sales and lease comparables described in the body of the report are shown in detail on the comparable sheets included in the addenda. Market data was obtained from the following resources:

- Lewis and Clark County Clerk and Recorder's Office
- Lewis and Clark County Treasurers Office
- City of Helena Planning Department
- Joe Moore, Appraiser
- Tim Moore, Appraiser
- Randall Green, Realtor
- Peter McNamee, Property Owner
- John Craig, Property Owner
- Gary Frederick, Realtor
- Buck Rea, Property Manager
- Alan Bock, Realtor
- Steve Nistler, Realtor
- James Burrington, Property Owner

- Marta George, Property Manager
- Larry Hayes, Property Owner

Effective Date:

The effective date of this appraisal is December 23, 2013. This is the date of valuation and was the actual date of the property inspection. It is also the date all enclosed photographs of the subject property were taken. This appraisal report was completed on December 31, 2013. Market conditions have remained effectively unchanged between the effective date of appraisal and the completion date of the written report.

DEFINITION OF MARKET VALUE

Market value, as used in this report is defined as follows:

“The most probable price, as of a specified date, in cash, or in terms equivalent to cash, or in other precisely revealed terms, for which the specified property rights should sell after reasonable exposure in a competitive market under all conditions requisite to a fair sale, with the buyer and seller each acting prudently, knowledgeably, and for self interest, and assuming that neither is under undue duress.”¹

Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

1. Buyer and seller are typically motivated;
2. Both parties are well informed or well advised, and acting in what they consider their own best interests;
3. A reasonable time is allowed for exposure in the open market;
4. Payment is made in terms of cash in United States dollars or in terms of financial arrangements comparable thereto; and
5. The price represents the normal consideration of the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with this sale.

¹ *The Appraisal of Real Estate, 12th Edition*, (Appraisal Institute, 2001), p. 22.

PURPOSE OF THE APPRAISAL

The purpose of this appraisal report is to arrive at a supportable estimation of the market value.

INTENDED USE OF THE APPRAISAL AND INTENDED CLIENT

It is understood that the intended use of this appraisal report is to assist the client with internal decisions regarding the future use of this property. The user of this appraisal report is the State of Montana, Department of Natural Resources & Conservation, Trust Land Management Division.

PROPERTY RIGHTS APPRAISED

This appraisal is made with the understanding and assumption that present ownership of the subject property includes all rights that may be lawfully owned, and is therefore, title in fee simple as of December 21, 2013. A fee simple estate is subject only to the limitations imposed by the governmental powers of taxation, eminent domain, police power and escheat.

IDENTIFICATION OF PROPERTY AND LEGAL DESCRIPTION

The property which is the subject matter of this appraisal report is a professional office building on a 60,000 SF site. The property is addressed 1539 11th Avenue in Helena, Montana.

The legal description of the land involved is as follows:

"Lot D, Block 21, Cannon CW Addition to the City of Helena, Lewis and Clark County, Montana."

PURPORTED OWNER

An investigation was made at the Lewis and Clark County Courthouse Clerk and Recorder's Office, State of Montana. Records within that Office indicate that the State of Montana is the current owner of record. This is shown on the Warranty Deed dated July 8, 1981. A copy of this deed is contained in the addenda.

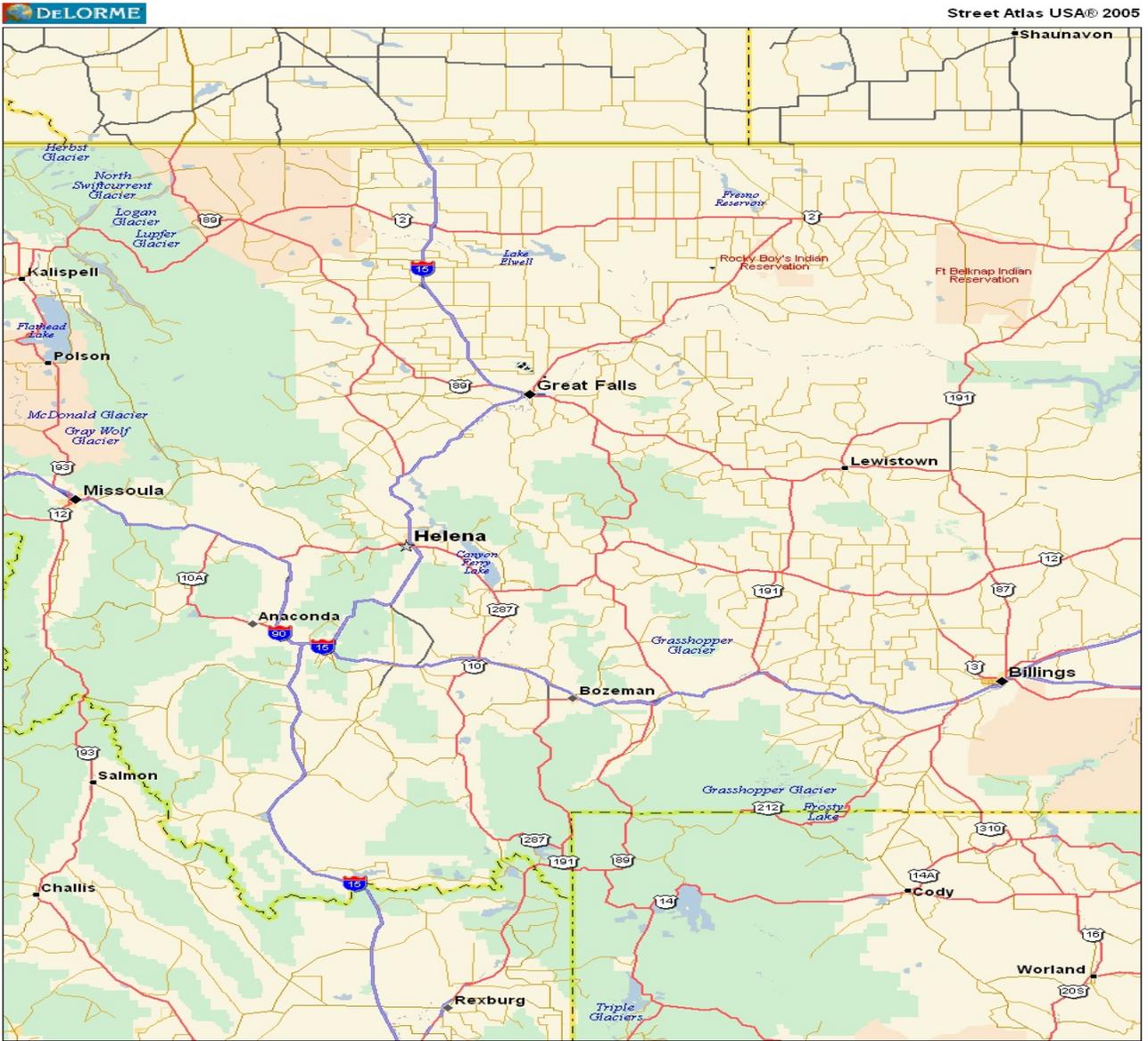
SALES HISTORY OF THE PROPERTY

It was confirmed at the time of my site inspection that the State of Montana purchased this property in 1981 and its employees have occupied this building since. To the best of my knowledge this property is not currently listed for sale.

PERSONAL PROPERTY

All mechanical equipment such as plumbing fixtures, electrical fixtures, heating equipment, built-in cabinetry, wall coverings and carpet as finish flooring is considered to be a part of the real estate. There are no items of personal property included in this appraisal report.

REGIONAL MAP



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www.delorme.com

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MN (0.0° W)

0 16 32 48 64 80 mi
Data Zoom 8-2

REGIONAL AND CITY ANALYSIS

Helena is the county seat of Lewis and Clark County and the state capitol of Montana. Lewis and Clark County is one of 56 counties in the state of Montana, and is located on the front range of the Rocky Mountains in south central Montana. Helena is centrally located at the junction of Interstate 15, and US Highways 12 and 287. This is halfway between Glacier and Yellowstone National Parks, both major attractions to the state of Montana.

Lewis and Clark County, Helena in particular, has historically experienced stable economic conditions. Montana in general is known for its farming, agricultural, mining, and tourism industries. Helena, while enjoying the benefits of these industries, also sees the stability from being the county seat and the state capitol. Helena has not experienced the boom and bust cycles that have effected many other Montana communities. In addition to being the political center for the state of Montana, Helena thrives as an educational, commercial, recreational and cultural center.

Forces Influencing Property Values

The value of real estate is influenced by the interaction of four major forces. Social considerations, economic considerations, government and environmental considerations. The four forces are discussed as follows:

Social Considerations

Social forces are exerted largely by population characteristics, including population growth, density, and age distribution. The population within the Helena city limits is 28,726 people, and Lewis and Clark County is nearly 56,000 people. The tri-county area includes the Helena city limits and the surrounding valley, and the adjacent bedroom communities in North Jefferson County and West Broadwater County. This tri-county area has a population of approximately 70,000 people. Helena and its surrounding communities, like much of Montana, has seen an influx of people from the neighboring northwest states. Overcrowding in larger cities has influenced moving to areas that offer smaller, and often safer communities. Like much of Montana, Helena is viewed as a more affordable area to reside in, and also offers a very attractive physical environment. Census figures show Helena's population increased from 27,592 in 2005 to 28,592 in 2011. This is a 3.62% change in population. The median resident age is 39.2 years and the median household income is \$47,744. The average sales price of residential real estate in June, 2008 was \$220,117, and as of April, 2013 was \$239,950 which is a 9.01% increase. These figures all show

that Helena is showing slow but stable growth in its population, income levels and real estate values.

Montana has a wide variety of outdoor recreational opportunities. The Missouri River, Canyon Ferry Lake, Hauser Lake, and Holter Lake are all near Helena providing excellent recreational opportunities. Vast public lands are also available within the region providing numerous opportunities for big game hunters, outfitters, hikers, backpackers, alpine skiers, and the use of snow machines. There are a number of ski hills that range from small, locally owned and operated to Big Sky Resort near Bozeman which is one of the largest ski hills in this region.

The City of Helena has 25 city parks, three golf courses, and 17 public tennis courts. Also, a number of facilities offering cultural events are in the city limits.

Economic Considerations

Helena, like the rest of Montana and most of the United States, has been experiencing growth of its economy for the past several years. In the long run, the outlook for Helena and the vicinity is quite positive based on a number of factors.

- County seat of Lewis and Clark County, and the state capitol of Montana.
- Central location
- Influx of population
- Wide range of skills in the labor force

In addition to the large state and federal government employment base, Helena has a diversified skilled labor force. As community expansion continually creates new employment, unemployment rates have typically averaged approximately ½% below the state of Montana rate, and almost 1% below the national average rate. As of February, 2013 the unemployment rate for the United States was 7.6% and Montana's unemployment rate was at 5.6%. Helena had experienced several years of rapid residential and commercial expansion. Residential expansion was seen north and east of the Helena city limits due to the lack of available vacant land within the city limits. Commercial construction has been prevalent throughout the city limits where land is available. Several large discount stores, banking facilities, automobile centers, numerous strip centers and multi family developments have occurred. New commercial properties require occupancy which is causing a higher vacancy rate in several established older neighborhoods. Lower rental rates and/or renovation of some buildings is being seen to keep occupancy rates higher. Some areas have been unaffected and have not seen a decrease in rent levels. Property values have slowly appreciated and sales activity has remained stable. Helena's economy, and Montana's economy in general, is considered to be stable and is currently experiencing mild to moderate growth at $\pm 3\%$ per year.

Governmental Considerations

The City of Helena enjoys good quality police and fire protection with 43 full-time police officers, and 36 full-time firemen. The city government has a mayor, four city commissioners, and a city manager. Adequate schools are available at all levels of education with 11 schools being either elementary or middle schools, two private high schools and two public high schools. Secondary education is provided by Carroll College which is a private college, or the Helena College of Technology which is associated with the University of Montana.

Helena's zoning ordinance and building codes are consistent with guidelines required for responsible construction quality and orderly growth in defined areas. All city services and utilities are available.

Property taxes are administered by the city, county, and school districts for which the property is located. There is no sales tax in Montana.

Environmental Considerations

Environmental and physical forces, both natural and man made, can influence property values. These forces include climatic conditions, topography and natural barriers, and transportation systems.

The climate near Helena can best be described as modified continental. Continental climate means the summers are dry and hot, and the winters are cold. However, Helena has affectionately been called the banana belt of Montana. Due to a series of surrounding mountain ranges, Helena is often spared the prolonged bitter and cold winters. The average high temperature in January is 29°, the average high temperature in July is 85°, and the average annual precipitation is 12.12 inches. A milder climate helps reduce operating costs for business, and furthermore it helps to extend the effective life for many buildings.

Helena is located at the juncture of Interstate 15 and US Highways 12 and 287 which allows for easy travel in all directions. Several commercial and charter airlines provide air service to the Helena area. There are commercial and charter bus services, motor carriers, and two railroads.

Parts of Montana are subject to seismic activity which has been minimal and apparently not effected property values.

Conclusion

The large government presence coupled with a wide variety of small businesses has allowed Helena to experience positive economic conditions in years past. Nationally the economy has slowed and quite significantly in some areas, which has affected this area as well. It is expected real estate values in Helena will generally remain stable or see moderate growth while the economy on a local and national basis can correct itself.

marketability over the years. Over the past 10-15 years this neighborhood was going through a revitalization cycle with many of the older properties being remodeled or removed and developed with a higher and better use.

The value of real estate is influenced by the interaction of four major forces: social considerations, economic considerations, governmental considerations, and environmental considerations. These four forces are discussed as follows:

Social Considerations

Neighborhood occupants are often attracted to a location for its status, physical environment, services, affordability, and convenience. This neighborhood is easily accessible from surrounding Helena neighborhoods. 11th Avenue and Prospect Avenue, two main thoroughfares, and Interstate 15 provide good access from all directions. The traffic volume in this neighborhood is among the City's highest. Other areas within the city limits feature higher traffic counts but they typically do not have the sustained high traffic volume found in this neighborhood. Within the neighborhood boundaries shopping is readily available, and churches and schools (K-grade 12) are nearby. The central business district is within one mile to the west, and numerous recreational and cultural facilities are available within a three mile radius.

Typical occupants of the neighborhood are professional business persons. There is not an abundance of litter or graffiti, and the crime level is considered low as most of Helena is.

Economic Considerations

Economic considerations of a neighborhood relate to the financial capacity of the occupants, and their ability to rent or own property, to maintain it in an attractive and desirable condition, and to renovate or rehabilitate when it is needed. This neighborhood has a good mix of owner occupied and leased buildings, and the values range greatly due to the vast mix of property types. Rental properties had historically seen strong demand because of the proximity to the state capitol complex and access to the adjoining neighborhoods.

Sales information within this developed neighborhood is limited. The neighborhoods good location and historical low vacancy rates has attributed to a low turnover of ownership. New construction within the neighborhood has transpired by razing existing properties to make way for new buildings. The neighborhood is primarily built up as there is little or no vacant land available. The Capitol Hill Mall has steadily been losing its tenants and the underlying land is nearing a change in its use.

Property age ranges from new to \pm 100 years. Buildings typically show good maintenance and upkeep, with effective ages less than actual age.

Governmental Considerations

Governmental considerations relate to the laws, regulation, and taxes that affect neighborhood properties, and the administration and enforcement of these constraints. The tax burden for this neighborhood is typical to other commercial oriented neighborhoods within the Helena city limits. The quality of fire and police protection is considered good, adequate schooling facilities are available in the immediate area, and all utilities are readily available. Streets are adequately maintained. They are plowed in the winter months and swept in the summer months. There is no known special improvement district assessments within the neighborhood, nor outstanding against the subject property.

Zoning ordinance and building codes for the city of Helena are consistent with surrounding neighborhoods and have enforced responsible construction quality and orderly growth within the neighborhood boundaries.

Environmental Consideration

Environmental considerations consist of any natural or man made features that are contained in or effect the neighborhood in its geographic location.

The neighborhood topography is generally level which typically equates to less cost per square foot at construction, easier property maintenance, and easier maintenance of the roads throughout the neighborhood.

Lot size and shapes vary throughout the neighborhood, however land use patterns remain fairly consistent with professional office, retail, and shopping centers. Generally properties are well maintained within the neighborhood.

Natural gas, electricity, water and sewer services, telephone services, and cable television services are readily available within the neighborhood.

Access to schools, shopping, parks, recreational facilities, churches, and employment is good as each of these are nearby or within the neighborhood boundaries.

There are no known detrimental influences, nuisances, or hazards affecting the subjects neighborhood.

Conclusion

This neighborhood was once one of the more desirable commercial oriented neighborhoods within the Helena city limits. This neighborhood still has good access to surrounding neighborhoods, other community facilities, and has excellent transportation routes. However, in recent years there has been significant new retail development approximately two miles to the north at the Interstate 15 and Custer Avenue interchange. Most new office building development is taking place in the Great Northern Town Center which lies at the northern edge of Helena's CBD. Office and retail rent in the subject's neighborhood have a wide range but for the most part are consistent with other areas of Helena that have older office and retail buildings. This neighborhood's proximity to the State Capitol campus has always been one of its most marketable features.

The Capital Hill Mall, considered the hub of this neighborhood for many years, has steadily been losing its tenants and is nearing a change in use. It is expected the land that supports the Capital Hill Mall will be redeveloped to its highest and best use once the building improvements are no longer being used, which is similar to the scenario at the subject property. It is my opinion market values for the most part will remain stable in this neighborhood as the economy slowly continues to correct itself.

REAL ESTATE TAXES

The Montana State Department of Revenue, working through each county courthouse, appraises all taxable real estate, presumably at market value. State law has prescribed that a re-evaluation plan be completed periodically. The most recent Statewide reappraisal was completed in July, 2008, which is for tax years 2009 thru 2015. Single family dwellings are predominately valued based upon the sales comparison approach. When market data proves to be unreliable, Montana Department of Revenue appraiser's will use replacement cost, less depreciation. For commercial property, the appraisers have relied most heavily on the cost approach, but in areas where sufficient income and expense data is available, the income approach is being considered more and more. The Marshall Valuation Service Cost Manual is heavily used by the Montana Department of Revenue appraisers. Other non-public data, resulting from the Real Estate Financial Disclosure Act, is also considered.

Due to the fact that the Department of Revenues values are based upon pre 2008 market data, the current market values may or may not be indicative of the value for tax purposes depending on the changing market conditions. The Montana Legislature has recognized that real estate values have been increasing significantly, therefore, it enacted into law a phase-in process along with a value exemption for residential and commercial property. The phase-in process for the current reappraisal cycle is 16.66% per year for both classes of property. The exemption for residential property is 36.80% for tax year 2009 and increases incrementally to 47% for the succeeding years. The exemption for commercial property is 14.20% for tax year 2009 and increases incrementally to 21.50% for the succeeding years. The market value depicted on the tax statements is the value after the phase-in and exemption adjustment. This value is also referred to as the "Taxable Market Value". The tax rate is then applied to the taxable market value to establish the taxable value. The tax rate for 2009 is 2.93% and is adjusted downward annually, until it reaches 2.47% in 2015. Each of these adjustments to the Department of Revenues market value determination is an attempt to keep real estate taxes relatively equal to previous tax years. The final step in determining the general property tax is by multiplying the taxable value by the jurisdictional mill levy. The following table illustrates **examples** of how the taxes are determined for a residential and a commercial property:

Example 1		Example 2	
Residential Property Tax Calculation		Commercial Property Tax Calculation	
\$80,000	2003 full reappraisal value	\$1,900,000	2003 full reappraisal value
-\$60,000	2002 value before reappraisal increase	-\$1,200,00	2002 value before reappraisal increase
\$ 20,000	from reappraisal	\$ 700,000	from reappraisal
x 1.00	16.66% phase-in of increase per year	x 1.00	16.66% phase-in of increase per year
\$20,000	x 6 years (16.66% x 6 = 100%)	\$ 700,000	x 6 years (16.66% x 6 = 100%)
+\$60,000	2002 value before reappraisal	+\$1,200,000	2002 value before reappraisal
\$80,000	2008 phase-in value	\$1,900,000	2008 phase-in value
x .660	2008 homestead exemption (34%)	x .850	2008 comestead exemption (15%)
\$52,800	2008 taxable market value (TMV)	\$1,615,000	2008 taxable market value(TMV)
x .0301	(3.01%) tax rate	x .0301	(3.01%) tax rate
\$ 1,589	taxable value (approx.)	\$ 48,611	taxable value (approx.)
x .500	(500 mills) mill levy*	x .500	(00 mills) mill levy*
\$ 794	general property tax (approx.)	\$ 24,305	general property tax (approx.)
This example is for illustrative purposes only. Mill levies vary by school district and taxing jurisdiction.			

The tax bill sets forth the taxable market values and taxable values for both the land and improvements. As noted above the mill levy is applied against taxable value to obtain the dollar amount of general taxes. General taxes and perpetual improvement district charges are listed for the first and second halves of the year. Real estate taxes are paid in arrears, with the first half due in November of the current year and the second half due in May of the following year.

The subject property is owned by the State of Montana which is a tax exempt entity. The subject property is assessed for a variety of city charges i.e. street maintenance, water quality, etc. The total tax bill for 2012 is \$1,610.10 As of the effective date of this appraisal report there are no outstanding charges to the subject property and there are no outstanding short term special improvement district (SID's) assessments applicable to the subject property.

If the subject property were sold to a private entity real estate taxes would be levied against this property. Therefore to complete my market value estimate it is necessary to estimate the tax liability for the subject property. I have identified similar commercial properties used in the following market analysis and it was determined that \$1.00/SF of the building area or \$25,000 per year is an appropriate estimation of the real estate taxes for the subject property.

PLOT PLAN

PROPERTY DESCRIPTION

Site

Size:

There is 200' of frontage on 11th Avenue and 9th Avenue and this site has a depth of 300' for a total area of 60,000 SF. The building and its site improvements function on 47,878 SF because 12,122 SF in the SEC is leased to the adjacent property owner. The market value of the 47,878 SF portion of the site will be estimated and the contributory value of the leased portion of this site will also be estimated.

Shape:

Rectangular

Topography:

This site is essentially at grade with 9th Avenue along its south boundary. The land mildly down slopes to the north towards 11th Avenue and is elevated slightly above 11th Avenue.

Soil Conditions:

Soil conditions are unknown. No soils test was provided to your appraiser.

Access/Easements:

The primary access to this property is off of 9th Avenue which leads directly to the paved parking lot and the main entrance to the building on its south side. There is an access off of 11th Avenue which connects to a driveway that circulates traffic around the SEC of the building.

To the best of my knowledge there are no easements or encroachments that adversely affect the value of this site. A copy of a pipeline easement for natural gas that was recently signed was provided to me and is included in the addenda. A title policy should be used for the final determination of easements and encroachments on this property.

Utilities:

The site is serviced by city water and sewer, natural gas and electricity.

Location/Visibility:

This site extends between 11th Avenue and 9th Avenue and is approximately 1 block east of Sanders Street. This site has good visibility for east bound traffic on 11th Avenue which is a one-way traffic street and is also the Highway 12 East thorough fare. The intersection of 11th Avenue and Sanders Street (approximately 1 block to the west) is a lighted intersection. This site is located approximately 6 blocks west of Interstate 15.

Functional Adequacy:

This site is well suited for development with a commercial building. The land lease that encumbers the SEC of this site appears to be more of a detriment than an advantage to this property which is explained further in the following analysis.

Flood Plain:

The subject property is located in an area that does not have a flood map printed. This area is indicated to be in Flood Zone C which is an area of minimal flooding and designated outside of the 100 year flood plain. The FEMA Map Panel number is 300040 0005B. This map is dated April 15, 1981.

Nuisances or Hazards:

The subject site is generally surrounded by other office or retail uses on the east, south and west sides. The State Capitol complex is 3 blocks to the south. The Capitol Hill Mall lies directly across 11th Avenue which has seen a number of recent vacancies and appears to be nearing a change in its use.

Site Improvements

There are concrete walks around the perimeter of the office building and there is a large paved parking lot that lies south of the building and is accessed off of 9th Avenue. I counted 59 marked parking spaces on this property. This parking lot is elevated above the main entrance to the building. A set of concrete stairs and a retaining wall have been constructed between the parking lot and the main entrance to the building.

A paved driveway provides access from 11th Avenue and circulates around the east side and south side of the building. There is a large lawn area, mature trees and shrubs along the front and west side of the building.



Access off of 9th Avenue along the south property boundary



View of the parking lot behind the building improvements.



View of the concrete staircase and retaining wall between the parking lot and the building improvements.



Access off of 11th Avenue along the north property boundary.



View of the driveway that comes from 11th Avenue around the east and south sides of the building.



Looking south at the land that is leased to the adjoining property owner.



Looking north at the land that is leased to the adjoining property owner.

Building Improvements

Type and Size:

This building is a four level, brick office building. I measured the basement level at 7,352 SF, the first level at 7,352 SF, the second level at 6,680 SF and the third level at 3,624 SF for a total of 25,008 SF. According to the county records this building was constructed in 1900.

Quality of Construction:

Average

Footings and Foundation:

Concrete.

Floor Structure:

Concrete in the basement, wood sub-floors on the 2nd, 3rd and 4th levels.

Exterior Walls:

Brick

Roof Framing:

Wood frame.

Roof Cover:

Class B cedar shingles that were installed in 1981.

Windows:

A combination of aluminum frame and vinyl sliding windows.



Looking southwest at the subject property from 11th Avenue.



Looking southeast at the subject property from 11th Avenue.



East end of the building.



South side of the building and the main entrance.



Exterior boiler room access at the rear of the building.



Stairs on the north side of the building that were once the main entrance. This is no longer an entry to this building.

Interior Finish and Rooms:

The interior finish of this building is dated, the carpets are worn and the interior is in need of paint. There is carpet throughout this building with the exception of the restrooms and they have sheet vinyl flooring. The interior walls are a combination of plaster, drywall and wood paneling, and a brick finish is in the Director's office. Most of the ceilings are finished with 2' x 4' acoustical ceiling tiles however some of the ceilings are finished with sheet rock. This building is heated with a hot water boiler system and each office has an individual radiator. The radiators in the basement are much newer than those on the 2nd, 3rd and 4th levels. There is not an air conditioning system in this building. There is an elevator that provides access to each level of this building, and stairwells at the east and west ends.

It was confirmed at the time of my site inspection that this building has not received any significant renovation in recent years. It was explained the temperatures can be difficult to control in this old building and it can be cool in the winter months and very warm during the summer months because there is no air conditioning. The first level of this building is a subterranean basement that is a mix of office and storage space. The original kitchen, ½ bathroom and an old walk-in cooler still remain in the basement or first level. Some of the offices in this building are quite small while others require passing through one office to get to another. There are offices with no windows, and some of the offices on the 4th level have low and angling ceilings because of the roof lines. The hallways in this building are very wide, and like many of the features previously described, are typical to an office building of this vintage.

Overall the deficiencies in the floor plan, lack of recent renovations and its current condition make for average grade office space which

is reflected in the potential gross income estimate in the Income Approach to follow. A copy of the floor plan for this building is included in the addenda.

At the time of my site inspection the electrical service was still on however the water service has been shut off and reportedly the building has been winterized. The natural gas service is also shut off and therefore the building was not heated. John Grimm reported to me that this building has been without water service and heat for approximately one year.



Typical 1st level (basement) office.



Kitchen area in the first (basement) level.



Storage room on the 1st level.



Typical 2nd level office.



Second level hallway.



View of the elevator and its hallway



Director's office on the 2nd level.



Men's room on the 3rd level.



Typical office on the 3rd level.



Fourth level office.



Stairwell off of the 4th level..



Interior view of the boiler room which is on the basement level but has an exterior access.

ZONING

Investigation at the Helena City County Building indicated that the subject site is presently zoned "B-2" - General Commercial District. The General Commercial District is intended to provide for a broad range of commercial operations and service and for proper and convenient commercial centers serving large areas of the City. Permitted uses should include those retail and service operations that may be appropriately located within a shopping district and that are normally required to sustain a community.

Permitted uses include general merchandise stores, food stores, automobile dealers, service stations, apparel and accessory stores, furniture and home furnishings, eating and drinking places and miscellaneous retail stores including drug stores, miscellaneous shopping goods stores and miscellaneous retail stores. Also included are office uses for insurance, real estate, investment and personal services. Thus, all of the current uses and those uses for which the building improvements are best suited are permitted under the B-2 zoning.

Each lot in this district shall contain not less than 2,500 SF and no lot shall be less than 25' wide. In this district, buildings may cover the entire lot except for those portions constituting the yards, loading births, parking areas and landscaped areas required by this chapter. Front yards shall be at least 15' in depth, rear yards shall be 15' if abutting a residential district. No site yards are required except if the property abuts a residential district, the side yards shall be 10' in depth. No building in this district shall be higher than 34' unless a conditional use is granted. Off-street loading births shall be provided in accordance with the requirements of Chapter 22 of this Title. Off-street parking shall be provided in accordance with Chapter 22. Signs shall conform to the requirements of Chapter 23. Landscaping shall be provided in accordance with the requirements of Chapter 24. Subject property meets all zoning requirements and a copy of the B-2 zoning ordinance is in the addenda.

HIGHEST AND BEST USE

"The reasonably probable and legal use of vacant land or an improved property that is physically possible, appropriately supported, financially feasible and that results in the highest value."²

The definition above applies to the highest and best use of vacant land or improved property. It is to be recognized that in cases where a site has existing improvements on it, the highest and best use may very well be determined to be different from the existing use. The existing use will continue, however, unless and until land value in its highest and best use exceeds the total value of the property in its existing use.

Quite often in estimating the highest and best use of land, the appraiser is controlled by governmental regulations. These controls are generally zoning ordinance, parking requirements and building codes. Also, in the estimate of highest and best use, one must recognize the attitude of typical investors in the marketplace.

Real estate will usually fall into certain definite development patterns, and their uses can be classified as: residential, agricultural, recreational, industrial, commercial and public use. In valuing the highest and best use of the land both as if vacant and improved, the following criteria must be met. 1) legally permissible, 2) physically possible, 3) financially feasible, and 4) maximally productive.

Highest & Best Use of Land as Vacant

Legally Permissible

The subject property is zoned B-2 (General Commercial District). The intent of this district is to provide for a broad range of convenient commercial centers, serving large areas of the City. The B-2 zoning ordinance does not allow agricultural, recreational, industrial, or single family households, and therefore these uses can be eliminated.

Physically Possible

This neighborhood is improved with a mix of retail and office use. Most of the sites are improved to maximum density permitted by zoning while taking into account the parking and landscaping requirements. The sites best attribute is its location on 11th Avenue and being 6 blocks from Interstate 15. The subject site has good frontage along 11th Avenue with good depth and overall size. Its generally level topography and

² *The Appraisal of Real Estate, 12th Edition*, (Appraisal Institute, 2001), p. 305.

rectangular shape eliminate higher development costs associated with steep and irregular shaped sites. Access to the site is good and all public utilities are readily available. Soil conditions in the area have been proven adequate for development for all property types. Based upon the physical characteristics of the subject site and existing properties within the neighborhood, the legally permissible uses permitted by the B-2 zoning ordinance would be physically possible.

Financially Feasible

Helena, like most communities, had been experiencing appreciating market values and good growth for a number of years. This neighborhood was seeing strong demand because of its good location however new development has been limited because of the lack of vacant land.

It will be shown in the following analysis that the financially feasible use of the subject site is for a commercial use that is legally permissible and physically possible. Considering the sites location the most likely use of the site is for a retail or professional office use.

Maximally Productive

The uses that conform with the requirements of the first three tests and would provide the maximum productivity of the subject site is for a retail or office use.

Highest and Best Use of the Property as Improved

The subject property is zoned B-2 and the existing office building is a legally permissible use within that zoning ordinance. To the best of my knowledge the requirements for parking, landscaping, setbacks etc. conform with this zoning ordinance or are considered to be a nonconforming, legal use. This office building has functioned on this site for many years and obviously this is a physically possible use of these building improvements.

It will be shown in the following valuation section of this appraisal report that the existing building improvements are at the end of their economic life based upon the value of the underlying land. The existing building improvements are no longer the maximally productive use of this site. It will be shown that the highest and best use of the subject property is to raze the existing improvements to make way for a new and significantly more productive commercial building. When this is accomplished the property will become financially feasible and ultimately be maximally productive.

The State of Montana has taken some initial steps to redevelop this site which are addressed in the Memorandum dated January 25, 2012 that is included in the addenda. This Memorandum explains that officials from the State met with the City Zoning Office personnel and obtained the requirements to redevelop the 47,878 unencumbered portion of this site. It was explained that redevelopment of that portion of the site with a new building would essentially not be prevented by any of the current Helena zoning regulations.

PROPERTY VALUATION

Methods and/or Techniques Employed:

Whenever possible, all three basic approaches to value are utilized. The resulting indications of value are then correlated into a final estimate of market value. As discussed in the preceding Highest and Best Use Analysis it was explained that the highest and best use of this site is to raze the existing improvements to make way for a new and more productive commercial building. To demonstrate this the Sales Comparison Approach with respect to land value will be completed, then the Income Approach to Value will be completed which will show that the existing building improvements are no longer the financially feasible or the maximally productive use of this site. The Cost Approach to Value and the Sales Comparison Approach to Value for the building improvements are not completed because the building improvements are nearly fully depreciated and therefore these approaches to value are not found to be relevant.

SITE VALUATION

The method employed to value the site as if vacant and available for sale is the Sales Comparison Approach. An investigation of the market revealed several sales and listings indicative of what a well-informed buyer or seller would consider in forming an opinion of value. Four sales were chosen as being most appropriate to compare against the subject site. Descriptive data and photographs of these comparables are contained in the Addenda. First I will estimate the market value of the unencumbered 47,878 SF portion of this site and then estimate the contributory value of the leased portion of this site.

Adjustments

All comparables differ somewhat from each other, and from the subject in various ways. The usual differences are for cash equivalency, market conditions, location, and a number of physical characteristics. Many of these factors, in varying degrees, are applicable in the appraisal of the subject property. When dissimilarities are found in comparable properties, they are adjusted for by adding to the comparable price when the dissimilar factor is inferior to the same factor found in the subject property. Likewise, a minus adjustment should be made when the comparable sale has a factor which is superior to that found in the subject property. The sale properties, then, are adjusted to the subject property.

However, in the market it is often difficult and sometimes impossible to accurately isolate a given factor. In short, one very seldom finds sales which are identical in all respects but one, and thus is able to prove conclusively the value, or lack of it, for any one factor due to a difference in sale price. Often, there are plus and minus factors which offset each other. Thus, the use of subjective judgment, to some degree, may be exercised.

Nevertheless, the differences in values are real and adjustments based on as much fact as can be found, will be made. Then, the appraiser may call upon his experience to make subjective judgments.

Property Rights

Each of the sales involve fee simple property rights. As a result, no property rights adjustments were warranted.

Financing:

All Sales were cash to the seller or on terms considered cash equivalent, and no adjustments were required.

Conditions of Sale:

No non-market conditions motivating the buyer or seller involved in the transactions are known, therefore no adjustments are required.

Expenditures Immediately After Sale:

None of the sales required expenditures immediately after sale, and therefore no adjustments are required.

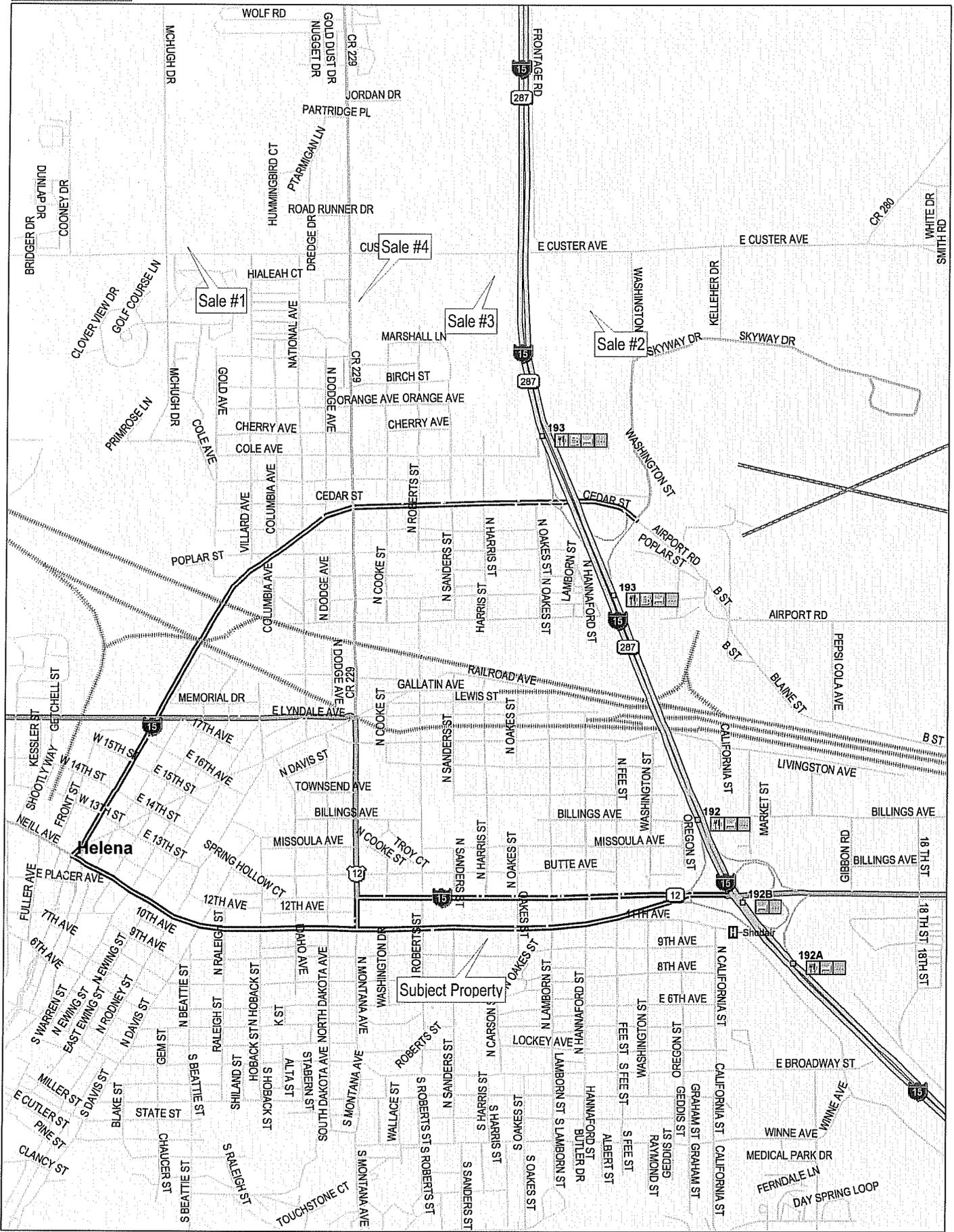
Market Conditions:

A market conditions (time adjustment) is required to bring all comparable sales up to the effective date of the appraisal report which is December 23, 2013. Market data indicates land values had been appreciating in and around the Helena city limits. I have in file a number of paired sales analysis that show market values were appreciating from approximately .75% to nearly 2% compound monthly appreciation. However, the local and certainly the national economy slowed and I found that sales that occurred after January 1, 2008 did not warrant a market conditions adjustment. Market values have more or less stabilized in Helena since the beginning of 2008 and in the past 12 to 18 months market activity has begun to increase again. I have not found enough current paired sales data to justify an appreciation adjustment in this market. The land sales used in this appraisal report sold in 2012 and 2013 and they all reflect current market values and therefore do not warrant a market conditions adjustment.

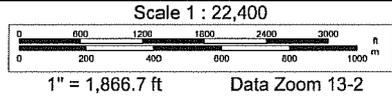
Remaining Adjustments:

The remaining adjustments will be explained in a qualitative analysis which is an effective technique that recognizes the inefficiencies of a real estate market and the difficulty in expressing the adjustments with mathematical precision. The adjustments included in the qualitative analysis are location, size, access, topography, utilities and zoning. The land sales adjustment grid can be seen on the following page.

LAND SALE LOCATION MAP



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LAND SALE ADJUSTMENT GRID

	SUBJECT	COMPARABLE 1	COMPARABLE 2	COMPARABLE 3	COMPARABLE 4
Sale Price		\$420,000	\$647,000	\$550,000	\$1,000,000
Size (SF)	47,878	30,000	46,217	44,344	57,940
Price/SF		\$14.00	\$14.00	\$12.40	\$17.26
Date of Sale		12/18/12	2/5/13	5/15/13	8/7/12
Market Adjustment		-0-	-0-	-0-	-0-
Adjusted Price		\$420,000	\$647,000	\$550,000	\$1,000,000
Adjusted Price/SF		\$14.00	\$14.00	\$12.40	\$17.26
Location	South side of 11th Ave. and 6 blocks west of I-15	North side of Custer Ave. and 5 blocks west of I-15	Cromwell Dixon Lane and 1 blk east of I-15	Sanders St. and adjacent to I-15	East side of N. Montana Ave., 2 blocks SW of I-15
Comparison		Similar	Slightly Superior	Superior	Superior
Size (SF)	47,878	30,000	46,217	44,344	57,940
Comparison		Slightly Superior	Similar	Similar	Similar
Access	11th Ave and 9th Ave.	Custer Ave.	Interior subdivision roads	Interior subdivision roads	Tara Court
Comparison		Similar	Slightly Inferior	Slightly Inferior	Slightly Inferior
Topography	Mostly Level	Mostly Level	Level	Level	Level
Comparison		Similar	Similar	Similar	Similar
Utilities	All city services	All city services	All city services	All city services	All city services
Comparison		Similar	Similar	Similar	Similar
Zoning	B-2	B-2	B-2	B-2	B-2
Comparison		Similar	Similar	Similar	Similar
Overall Comparability		Similar to Slightly Superior	Similar	Similar	Superior

J. Michael Joki, MAI, SRA
HELENA, MONTANA

Sales Analysis:

Comparable No.1 is a 30,000 SF site that sold for \$420,000 on December 18, 2012 or \$14.00/SF. As shown on the comparable sale sheet in the addenda this lot was one of three lots that sold in one transaction. This lot is located on the north side of Custer Avenue and approximately five blocks west of Interstate 15 which is a similar location when compared to the subject property. This site is slightly smaller than the subject property otherwise it is similar in all of its characteristics when compared to the subject site.

Comparable No. 2 is a 46,217 SF site sold on February 5, 2013 at \$647,000 or \$14.00/SF. This site is located on Cromwell Dixon Lane and approximately 1 block east of Interstate 15 and within the Skyway Regional Shopping Center which is anchored by Home Depot. As compared to the subject property this is considered to be a superior location. Comparable No. 2 is located approximately 1 block southwest of the Custer Avenue and Washington Street Intersection and is accessed from interior subdivision roads which is inferior when compared to the subject property. Comparable No. 2 is similar to the subject property in terms of its size, topography, utilities and zoning, and overall is considered to be similar to the subject property.

Comparable No. 3 is a 44,344 SF site that sold on May 15, 2013 \$550,000 or \$12.40/SF. Comparable No 3 is located on the east side of Sanders Street and adjacent to Interstate 15 which is a superior location when compared to the subject property. Comparable No. 3 is located in the Custer Landing Subdivision which is anchored by Office Depot, and like comparable No. 2 is accessed from interior subdivision roads. Comparable No. 3 is similar in its size, topography, utilities, and zoning when compared to the subject property, and overall is considered to be similar when compared to the subject property.

Comparable No. 4 is a 57,940 SF site that sold on August 7, 2012 at \$1,000,000 or \$17.26/SF. Comparable No. 4 is located on the east side of North Montana Avenue approximately 2 blocks southwest of Interstate 15 which is a superior location when compared to the subject property. In addition Comparable No. 4 is located at the intersection of Tara Court and North Montana Avenue which is a lighted intersection. Comparable No. 4 is similar in its size, topography, utilities and zoning when compared to the subject property, and overall is considered to be superior when compared to the subject property only because of its location.

All of the comparables have been given consideration in my final estimate of market value as they are all recent sales that recorded in either 2012 or 2013. All of these comparables are in proximity to Interstate 15 with Comparable No. 1 more or less having the same location as the subject property. Comparables No. 2, 3 and 4 are all similar in size when compared to the subject property and each of the comparables have slight variation in terms of their access. All of these comparables are similar to the subject property in terms of their topography, utilities and zoning. Considering this information it is my opinion the **unencumbered portion of the subject site** has a current market value of **\$14.00/SF**.

$$\begin{aligned} \$14.00 \times 47,878 \text{ SF} &= \$670,292 \\ &\$670,000(\text{R}) \end{aligned}$$

Contributory Value of the Leased Land

A copy of Lease No. 9446 is included in the addenda. This lease is between the State of Montana and Robert and Dolores Prescott wherein they are leasing 12,122 SF in the SEC of the subject site. The aerial photograph on page 4 highlights the approximate location of the leased land.

This lease agreement has a 15 year term which began on March 1, 2010 and will expire February 28, 2025. The annual rent is \$8,611.32 which is subject to a review and may be adjusted at the discretion of the Director of the Department of Natural Resources and Conservation at the end of the first five year period. Upon review the annual rent could be adjusted or remain the same, however no escalation clause is built into this lease agreement.

The leased land is properly identified as "excess land that is subject to a ground lease". Excess land, in regard to an improved site, is the land not needed to serve or support the existing improvements. The building improvements (25,008 SF) and its site improvements have functioned on the 47,878 SF portion of this property for many years. I have been told by several people that are directly familiar with this property that its access and on site parking have served this building well over the years. As previously noted in the Highest and Best Use Analysis the City of Helena Planning Department has explained that redevelopment of the 47,878 SF portion of this site appears to be reasonable. For these reasons the 12,122 SF portion of the site that is subject to the ground lease is excess land.

The land that is leased to the adjacent property owner has been leased for many years. A portion of their building improvements and their on site parking are on this 12, 122 SF site. This building has housed various restaurants over the past 25+ years. The land subject to the ground lease is an integral part of the use and operation of this restaurant building.

To determine the contributory value of this ground lease the income needs to be converted into an estimation of value. Because there is a steady rent payment over the 15 year term of this lease agreement a land capitalization rate will be used as opposed to discounting the income stream over the term of the lease. In the Helena market I have found land capitalization rates range between 8% and 11% which will vary depending on the tenant who is occupying the site, the length of the lease term and location/use of the site.

The portion of the subject site that is leased to the adjacent property owner is a key component to their building's use and operation. A portion of the restaurant building and most of its on site parking are within this 12,122 SF. Knowing this land is such an integral part of this building's operation and use lowers the likelihood that this tenant would default on this lease agreement. For these reason's an argument can be made that a land capitalization rate at the lower end of the range is reasonable because of the relatively low risk associated with this tenant. Comparable No. 3 used in the preceding land valuation analysis was available for lease at \$70,000/year. The site was listed for sale at \$650,000 and when dividing the lease rate of \$70,000 into the asking price of \$650,000 this indicated a land capitalization rate of 10.77%. While this land

capitalization rate is certainly at the upper end of the range Comparable No. 3 also includes the asphalt paving and concrete curbing in the parking lot which is certainly reflected in the annual lease amount. Ultimately this site was not leased and sold for \$550,000 and did not include any of the aforementioned parking lot improvements.

It is my opinion a reasonable land capitalization rate for the subject's ground lease is at the lower end of the range or 8%. Therefore the contributory value of the leased portion of the subject site is:

$$\begin{aligned} \$8,611.32 \div .08 &= \$107,642 \\ &\mathbf{\$108,000 (R)} \end{aligned}$$

The value indication at \$108,000 for this 12,122 SF site equates to \$8.91/SF. Obviously the land subject to the ground lease is rented below market rent because the value of the 47,878 SF portion of this site as estimated at \$14.00/SF. The below market rent is obviously favorable to the tenant and has created a leasehold value for the lessee. The ground lease will follow the subject property if it is ever sold and the current lease terms would be viewed as a detriment to this property as opposed to an advantage. If the SEC of this property was not leased this site could support a larger building footprint, house more on site parking, and "as if" vacant would be worth more on a square foot basis.

Site Valuation Recap

Unencumbered 47,878 SF :	\$670,000
Contributory value of the leased 12,122 SF	<u>\$108,000</u>
Total:	\$778,000

It will be shown that the estimated site value exceeds the indication of value via the Income Approach to follow. This justifies that the subject property is no longer functioning at its highest and best use.

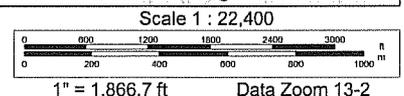
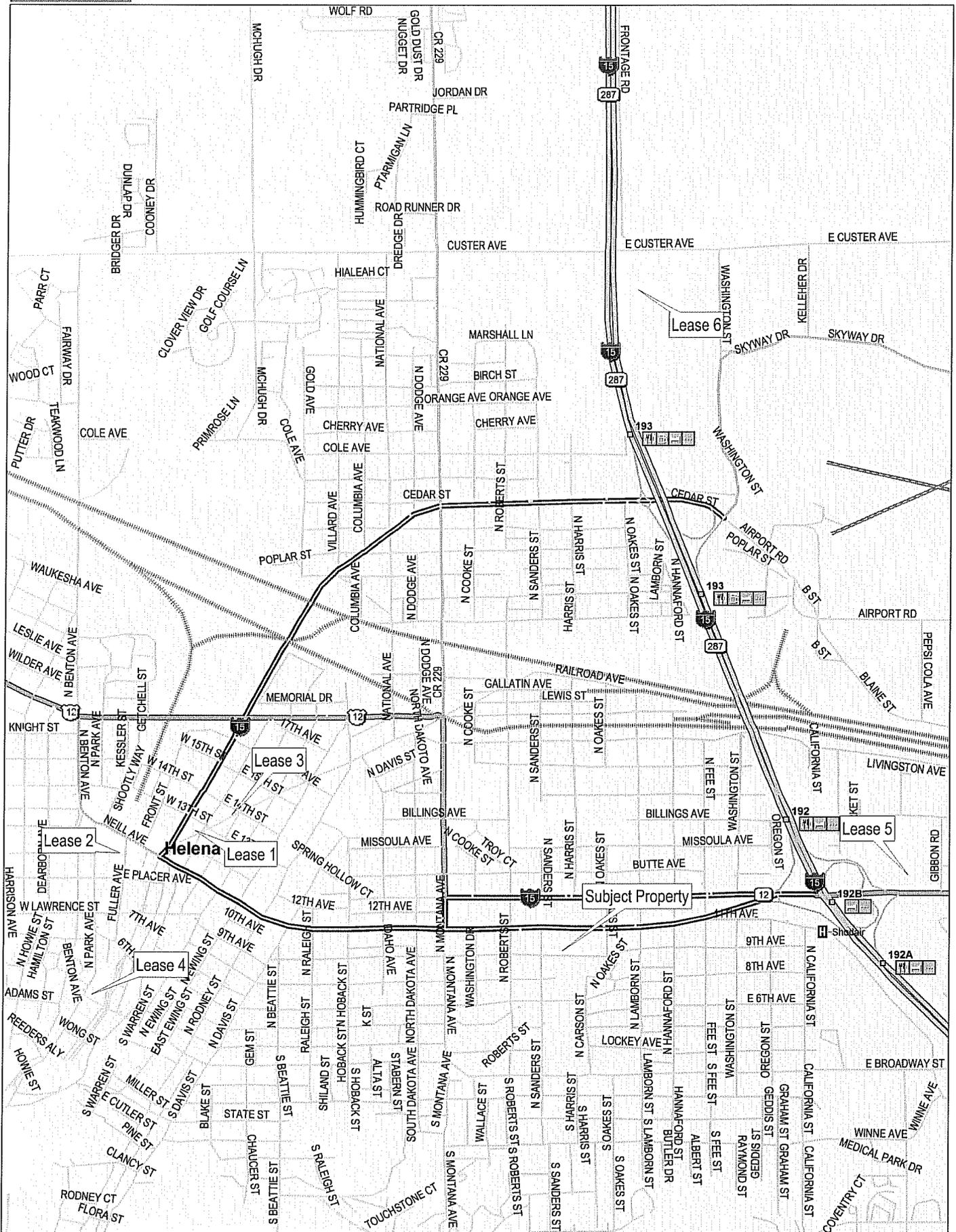
INCOME APPROACH

The Income Approach to value is based on the premise that market value is directly related to a property's future income-producing capabilities. Value has been defined in this context as "the present worth of future benefits." The market value of an income-producing property is, then, dependent upon the quality, quantity and durability of this income stream.

Gross Revenue Estimate:

The estimated gross revenue is typically derived through an analysis of the subject's past rental history and by conducting a rental survey of similar properties. The subject property has been occupied by various State agencies since 1981 when the State of Montana purchased this building. Since this building does not have a recent rental history it is necessary to survey the market in order to establish current rental rates for this office building. The following table and discussion is a summary of other offices buildings that are comparable alternatives to the subject property. In the addenda of this appraisal report are the comparable lease data sheets that outline the details of the comparable leases used in this analysis.

COMPARABLE RENTAL MAP



SUMMARY OF COMPARABLE LEASES

Lease No.	Name/ Location	Annual Rent	NLA/SF	Rent/SF	Lessor Pays	Lessee Pays
Subject	1539 11th Avenue, Helena		25,008 SF			
1.	618 Helena Ave., Helena	\$90,268	8,341 SF	\$10.82/SF	16	0
2.	555 Fuller Ave., Helena	\$131,300	10,000 SF	\$13.13/SF	16	0
3.	840 Helena Ave., Helena	\$135,281	9,803 SF	\$13.80/SF	16	0
4.	301 South Park Ave., Helena	\$696,223	52,065 SF	\$13.37/SF	16	0
5.	2550 Prospect Ave., Helena	\$168,739	15,370 SF	\$10.98/SF	16	0
6.	3075 N. Montana Ave., Helena	\$390,892	27,431 SF	\$14.25/SF	16	0

Legend: Lessor/Lessee Pays

0	None	6	Electricity	12	Janitorial in Common Areas
1	R.E. Tax	7	Gas (Heat)	13	Janitorial in Demised Space
2	Bldg. Insurance	8	Garbage	14	Snow Removal
3	Exterior Maint.	9	Parking Lot Maint.	15	Management
4	All Utilities	10	Interior Maint.	16	All
5	Water/Sewer	11	All Janitorial	17	All Other

Lease Analysis

The State of Montana occupies a large amount of professional office space within the City of Helena and it is not uncommon for the State to rent large areas. Garret Bacon, the leasing agent for the State, indicated some property owners may agree to some rent concessions as the State historically would enter into long term commitments, and the State of Montana is a quality tenant. The typical State lease agreement is predominantly configured on a gross basis wherein the lessor pays all operating expenses. In the capitalization process to follow the subject property will be valued on a gross basis, i.e., real estate taxes, building insurance, utilities, building maintenance, janitorial, reserves for replacement, garbage, and a typical cost for management will be deducted as lessor's expense. Thus, adjustments for "who pays what" are minimized when analyzing comparable leases. Each of the leases in the following discussion are configured on a gross basis and therefore no adjustments are required for the terms of these comparable lease agreements.

Lease No. 1 is located in the building addressed 618 Helena Avenue. This is a turn of the century, multi-story office building that houses several State agencies. Fish, Wildlife and Parks occupies 8, 341 SF on

the second level of this building. The rent for this space is currently \$10.82/SF and there are no escalation clauses over the term of this lease. This building is very similar to the subject property since it is an older, multi-story office building that has many of the same inefficiencies seen at the subject property. Overall this building is in similar condition when compared to the subject property.

Lease No. 2 is located at 555 Fuller Avenue which is a two story office building with a full basement. Public Health and Human Services (Addictive and Mental Disorders Division) occupies the first and second levels that total 10,000 SF. The rent is currently \$13.13/SF. This office building was constructed in 1949 however it has seen a number of recent renovations. Rents will escalate each of the last 3 years of this 5 year lease agreement. This comparable rental is an older office building however its recent renovations make this building in superior condition when compared to the subject property. This building's secondary location on Fuller Avenue is inferior to the subject's 11th Avenue location. Overall Lease Comparable No. 2 is considered to be similar to the subject property. This agency is looking to vacate this space but will sublease the space to another state agency at the same rent for the remaining term of the lease agreement.

Lease No. 3 is located at 840 Helena Avenue which is an older, 2-story office building that houses several State agencies. The Department of Labor and Industry (Job Service Workforce Center) occupies 9,803 SF in this building at \$13.80/SF. This building once functioned as a hospital and is now being used as office space. Like the subject property this building has some inefficiencies that are common in older buildings. Lease Comparable No. 3 is quite similar to the subject property in terms of its age, condition and overall location.

Lease No. 4 is located at 301 South Park Avenue which is a multi-story office building that is occupied by a number of State agencies. This building originally served as a federal courthouse building and since its construction has housed a number of State and Federal agencies. The property owner confirmed the rent for all of the State agencies occupying this building was negotiated to \$13.11/SF which is scheduled to escalate at 2% per year and is currently \$13.37/SF. This building is located at the very south end of Helena's Last Chance Gulch and when compared to the subject's location on 11th Avenue it is an inferior location. Lease Comparable No. 4 is a superior quality building that is in superior condition, and overall is considered to be superior when compared to the subject property.

Lease No. 5 is located at 2550 Prospect Avenue. This is a single story multi-tenant steel building that also occupies a number of State agencies. There are individual offices along the perimeter of the building however most of this space is open span that is best suited for cubicle work stations. Reportedly rents for this office were \$11.25/SF however the State of Montana requested that the rents be reduced to \$10.98/SF and there are no longer any escalation clauses in the lease agreement. Public Health and Human Services occupies

15,370 SF in this building at \$10.98/SF. Lease Comparable No. 5 has a similar location as it lies approximately ½ mile east of the subject property and overall is in similar condition when compared to the subject property.

Lease No. 6 is located at 3075 North Montana Avenue which is a single story, concrete masonry building that was renovated into office space in 1990 because it was previously used as a supermarket. This average quality building is now in above average condition and is currently being rented at \$14.25/SF. Lease Comparable No. 6 location on North Montana Avenue is similar to the subject's location, however this building is in superior condition and overall is considered to be superior when compared to the subject property.

The leases in this analysis are considered to be competitive alternatives for the subject property and range from \$10.82/SF to \$14.25/SF. All of these lease agreements are on a gross basis so no adjustments for terms were required. Most emphasis has been given to comparables No. 1, No. 2 and No. 3 as they are the most similar when compared to the subject property. Considering the age and condition/quality of the interior finish at the subject property it is my opinion a reasonable estimate of market rent is at the lower end of the range or \$11.00/SF. Applying this rental rate to the subject property suggests a potential gross income of:

$$\mathbf{\$11.00/SF \times 25,008 SF = \$ 275,088}$$

Vacancy and Credit Loss

There has been a considerable amount of commercial construction in the past several years in Helena, which includes a number of professional office buildings. There have been several new office buildings constructed in the Great Northern Town Center development that lies just north of Helena's original downtown area. Several other office buildings have also been constructed around Helena.

The subject property has predominantly been occupied by one State agency and most recently the Department of Corrections. Even though multiple tenants could occupy this building single tenancy is ideal if for no other reason than the climate control issues associated with this older building.

I have spoken with Garret Bacon, Leasing Officer for the State of Montana, and he explained there is currently no demand from the State of Montana for a ±25,000 SF building that is the age and condition of the subject property. While verifying market data it was found there is vacancy in other similar buildings in Helena and there is limited demand for their space either. A report recently completed by a local real estate broker estimated a vacancy factor of approximately 31% for office buildings in the Helena market. Reportedly the State of Montana does not currently have the funding to move its employees into newer office space at a higher rental rate. It was reported to me in years 2008/2009 the State of Montana leased nearly 100,000 SF of office space in Helena but very little new space has been leased since. Furthermore, many of the existing lease

agreements with the building owners were renegotiated and decreased anywhere from 5% to 30% which in some cases became below current market rents. The State of Montana has tried to renegotiate their lease agreements wherein there are no escalation clauses over the term of the lease, or in some cases it may be five to ten years before any escalation clauses are activated.

Considering that the subject property is already vacant and there is virtually no demand from the State of Montana or any private entities to fill this building with single tenancy, it appears that multi-tenancy would be the most reasonable way to fill this building. Considering all of these factors, I have estimated a reasonable vacancy and credit loss for the subject property is 25% to 30%. Another way to view this adjustment is a typical lease agreement in this market is 10 years and it is my opinion it would take about 2½ years before this building is fully occupied.

Expenses

I have been provided a 3 year expense history for the services that were contracted on this building for years 2009, 2010 and 2011. I confirmed with John Grimm that this is the most recent operating expense history for the subject property because this building has been “moth balled” for approximately one year and the water and heat are shut off, and minimal electricity is being used. The contracted services are for the elevator maintenance, janitorial service, mechanical equipment maintenance, garbage service, and the utilities which include gas, electric, water and sewer service. In 2011 the building had already been vacated and some of these expenses were significantly decreased. Therefore the operating expenses from years 2009 and 2010 have been relied upon because they are a more accurate reflection of these operating expenses when the building is fully occupied. A copy of this building expense sheet is included in the addenda. If a certain operating expense could not be provided to me by my client then data extracted from the market has been relied upon to determine the expense.

This property is owned by the State of Montana therefore it is exempt from paying real estate taxes. Because the fee simple interest is being appraised it is necessary to estimate the appropriate real estate taxes that would be paid by a typical property owner. I have estimated the real estate taxes for this building would be \$25,000 or approximately \$1.00/SF. While verifying the previously discussed lease comparables I found that \$1.00/SF is consistent with these similar, older office buildings in the Helena real estate market.

Property insurance also needs to be estimated from the market because all of the State buildings are self insured by the State of Montana. I have in file a number of insurance rates for office buildings around Helena that range from \$.15/SF to \$.49/SF. I estimated the insurance for this building at \$4,000 which equates to \$.16/SF and is certainly at the lower end of this range. I confirmed with a local insurance provider

that a \$4,000 annual premium is appropriate for this building.

A management expense must be accounted for with respect to over seeing the daily operation of the property. I have spoken with several property managers in the Helena area and it was indicated to me that a management fee will typically range from 5% to 7% for this type of building. Ideally this building would be occupied by a single tenant however the soft rental market for office space that currently exists in Helena could create multi-tenancy in this building. That being the case, a reasonable management expense for this building is estimated at 6% of the effective gross income.

The janitorial expense for years 2009 and 2010 was \$17,508 each year. This equates to \$.70/SF which appears to be below market. I have in file a number of janitorial expenses that range from \$1.00/SF to \$2.00/SF. For this building I have estimated the janitorial expense at \$1.25/SF.

Maintenance and repairs includes the building maintenance, elevator maintenance, snow removal and landscaping expenses. For years 2009 and 2010 these expenses were reported at \$17,520 or \$.70/SF. When compared to other building maintenance expenses I have on file for similar, older office buildings this amount appears to be reasonable. Another way to analyze the maintenance expense is to calculate it as a percentage of the effective gross income. This maintenance expense is 9.1% of the effective gross income which is also deemed as a reasonable amount for this expense item.

The utility expenses for 2009 and 2010 averaged \$34,550. This equates to \$1.38/SF and when compared to similar office buildings in Helena this amount appears to be reasonable.

Garbage expenses for 2009 and 2010 were reported at \$5,193 which appears reasonable for this building.

A replacement allowance is a typical expense item that normally needs to be accounted for. Typically property owners in Helena do not set aside funds for the replacement of the short lived items such as roof covering, floor covering, HVAC etc. Because these items have shorter lives than the structures, a reserve for their replacement must be recognized in order to accurately reflect ownership. Typically, each of the short lived items are given a replacement cost estimate, then a sinking fund factor is applied, which calculates the portion of the money required to set aside each year. However, for the subject property it has been determined that the improvements are nearing the end of their life and it could be argued that it is not necessary to set aside funds for the short lived items. However, since I am estimating the market value of this property this expense item will still be recognized. Another acceptable method to calculate the replacement allowance is to compute it as a percentage of the effective gross income. Considering the age of this building and its remaining economic life I will estimate a replacement allowance of 2% of the effective gross income for this building.

The estimated operating expenses for the subject property total \$132,928 or \$5.32/SF. On a square foot basis the operating expenses are actually at the lower end of the range for an older office building in this market

as they tend to range between \$6.00/SF and \$7.00/SF. The operating expense ratio is 69.03% and I found that most office buildings that are rented on a gross basis in this market range between 35% and 55%. However this is an old and expensive building to maintain and operate so the operating expense ratio of 69.03% is not entirely unheard of in this market. Also this calculation is a reflection of the lower market rent that would be obtained from this building.

Capitalization Rate:

The capitalization rate is one of the most critical factors in the Income Approach to value. Direct capitalization is utilized to convert an estimate of a single year's income expectancy into an indication of value in one direct step. The capitalization rate represents the relationship between income and value as observed in the market, and is a composite of the return "on" the investment as well as the return "of" the investment. It is also a means of measuring the quantity, quality, and durability of a property's income stream. The capitalization rate is derived from other investment properties which have recently sold by dividing the sales price into the net income of the comparable property at the time of its sale. As illustrated in the following table I've identified several building sales that were leased at the time of sale. The third and fourth sales are older office buildings located in downtown Helena with higher capitalization rates as a result of higher vacancy and greater operating expenses.

Property Address	2225 11th Ave.	2001 11th Ave.	555 Fuller Ave.	34 W. 6th Ave.	1151 Partridge Pl.
Effective Gross Income (EGI)	\$245,821	\$ 89,180	\$144,920	\$96,696	\$48,934
Less: Operating Expenses:	\$135,526	\$ 42,060	\$ 46,290	\$47,472	\$ 2,465
Net Operating Income (NOI)	\$110,295	\$ 47,120	\$ 98,630	\$49,224	\$46,469
NOI ÷ Sale Price = Overall	\$110,295/	\$47,120/	\$98,630/	\$49,224/	\$46,469/
Capitalization Rate	\$1,300,000	\$650,000	\$850,000	\$550,000	\$615,000
Overall Capitalization Rate	8.48%	7.25%	11.60%	8.95%	7.56%

The subject property is a large, older office building that has seen minimal updates over the years and is expensive to operate. The State of Montana has essentially put a moratorium on relocating their State agencies and the risk factor associated with a building like the subject property becomes considerably higher. It is my opinion an appropriate overall capitalization rate that reflects the risk associated with this property is 11%. Knowing there is virtually no demand for this office space at this time an argument could be made that a higher

overall capitalization rate could be justified for this property. However, the vacancy and credit loss estimate at 30% of the potential gross income reflects some of the short falls and risks associated with this property, which in my opinion justifies an 11% capitalization rate for this property.

Valuation

Potential Gross Income (PGI)	\$275,088
Vacancy & Collection Loss (30%)	(\$82,526)
Effective Gross Income (EGI)	\$192,562

Operating Expenses

Real Estate Taxes	\$25,000
Building Insurance	\$ 4,000
Management	\$11,554
Janitorial	\$31,260
Maintenance/Repairs	\$17,520
Utilities	\$34,550
Garbage	\$ 5,193
Reserves for Replacement	\$ 3,851
Total Operating Expenses	(\$132,928)
Net Operating Income (NOI)	\$59,634

$$\$59,634 \div .1100 = \$542,127$$

\$542,000 (R)

The contributory value of the leased portion of the subject site was previously estimated at \$108,000. This ground lease will follow the subject property if it is ever sold and therefore it is appropriate to add this value to the preceding Indication of Value from the Income Approach.

Recap of the Income Approach to Value

Value of the 47,878 SF site and its building improvements:	\$542,000
Contributory value of the leased land:	<u>\$108,000</u>
Total:	\$650,000

The indication of value from the Income Approach is \$650,000 which is less than the preceding value estimate of the subject site "as if" vacant at \$778,000. This indicates that the existing building improvements are no longer financially feasible and therefore are not the maximally productive use of this site. Maximum productivity of the subject site would be for redevelopment with a new office or retail building that is commensurate with the current land values in this neighborhood.

DEMOLITION COSTS

As previously discussed the estimated site value "as if" vacant is above the indication of value shown by the Income Approach which indicates that the building improvements are at the end of their life. This site needs to be redeveloped to a higher and better use.

Demolition costs need to be accounted for when it has been determined that the highest and best use of the site is to remove the existing improvements. I have spoke with two local contractors to determine a cost estimate for the demolition of the building improvements.

When I appraised the subject property in 2012 I spoke with Marty Shuma at Dick Anderson Construction and he provided a cost estimate of \$250,000 to demo this building. This is under the assumption there are no extraordinary measures needed to remove asbestos nor are there any costs associated with lead abatement. Mr. Shuma also provided the cost to remove and fill the basement area which ranged from \$75,000 to \$100,000. In total this cost estimate ranges from \$325,000 to \$350,000. I spoke with Marty Shuma again on December 26, 2013 and he estimated there would be a cost increase of 3% to 4% to demo this building which increases their cost range estimate to approximately \$335,000 up to \$365,000.

When I spoke with Phil Vinton from Diamond Construction in 2012 he gave me an overall cost to demo this building and backfill the basement area at \$350,000. This bid does not include any extraordinary costs associated with asbestos or lead abatement. Neither bid includes removing the asphalt from the existing parking lot. When I spoke to Phil Vinton on December 30, 2013 he explained his cost estimate would increase by 7% to 8% so the current cost to demo this building would range from \$375,000 to \$380,000.

Since both of these bids are very close it is my opinion the cost to demo this building is reasonably estimated at **\$370,000**. To determine an exact demolition cost both contractors explained they would need to enter the building so a more exact list of building materials could be compiled. Buildings of this age may contain levels of asbestos and other hazardous materials that may require special handling and disposal which in turn could alter the demolition costs.

VALUE ESTIMATE AND CERTIFICATION

The undersigned does hereby certify that, to the best of his knowledge and belief, except as otherwise noted in this appraisal report:

1. the statements of fact contained in this report are true and correct.
2. the reported analysis, opinions, and conclusions are limited only by the reported assumptions and limiting conditions and/or those found in the letter of engagement or appraisal consultation contract authorizing this report and are our personal, impartial, and unbiased professional analysis, opinions, and conclusions.
3. I have no present or prospective interest in the property that is the subject of this report, and I have no personal interest or bias with respect to the parties involved.
4. I previously appraised the subject property on March 6, 2012 for the Department of Natural Resources and Conservation Trust Land Management Division.
5. I have no bias with respect to the property that is the subject of this report or to the parties involved with this assignment.
6. my engagement in this assignment was not contingent upon developing or reporting predetermined results.
7. my compensation for completing this assignment is not contingent upon the development or reporting of a predetermined value or direction in value that favors the cause of the client, the amount of the value opinion, the attainment of a stipulated result, or the occurrence of a subsequent event directly related to the intended use of this appraisal. This appraisal assignment was not based on a requested minimum valuation, a specific valuation or the approval of a loan.
8. my analysis, opinions and conclusions were developed, and this report has been prepared, in conformity with The Uniform Standards of Professional Appraisal Practice and with the requirements of the Code of Professional Ethics and the Standards of Professional Practice of the Appraisal Institute.

9. the use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives.
10. as of the date of this report, I, J. Michael Joki, have completed the requirements of the continuing education program of the Appraisal Institute.
11. I have made a personal inspection of the property that is the subject of this report.
12. no one provided significant real property appraisal assistance to the person signing this appraisal report.
13. I, J. Michael Joki, am currently licensed in the State of Montana (Certificate #152) as a Certified General Real Estate Appraiser, and hold the MAI and SRA designation conferred by the Appraisal Institute. Regarding the Competency Provision of USPAP I further attest that over the past 25 years I have had substantial approved education and experience in the appraisal of residential and commercial properties. Specifically I have appraised a variety of office buildings in the Helena area.

Based upon all the elements of which I am aware and which could reasonably affect value, I have estimated the current market value of the subject property, as of December 23, 2013, to be:

SEVEN HUNDRED AND SEVENTY-EIGHT THOUSAND DOLLARS

\$778,000



December 31, 2013

Date

J. Michael Joki, MAI, SRA

ADDENDA

J. Michael Joki, MAI, SRA
HELENA, MONTANA