Clerk File No. [redacted] 310914

Appeal of 1507 Group, L.L.C. of a recommendation by the Hearing Examiner on landmark controls and incentives for the Eitel Building, 1501 Second Avenue (Quasi-judicial).

Related Legislation File: _____

Date Introduced and Referred:	To: (committee):
6.28.10	Built Environment
Date Re-referred:	To: (committee):
Date Re-referred:	To: (committee):
Date of Final Action: 1/31/11	Disposition: Appeal Denied, Approved Hearing Examiners Recommendation

6.23.10

Date Filed with City Clerk

By _____

The City of Seattle – Legislative Department

Clerk File sponsored by: no sponsor required

Committee Action:

Date	Recommendation	Vote
1/12/11	Deny Appeal, Approve Hearing Examiner's Recommendations	3 (Clark, Bagshaw, Burgess) - 0

This file is complete and ready for presentation to Full Council. _____

Full Council Action:

Date	Decision	Vote
1/31/11	Appeal Denied, Hearing Examiner's Recommendation Approved	9-0

CF No.310914

Title:Appeal of 1507 Group, L.L.C. of a recommendation by the Hearing Examiner on landmark controls and incentives for the Eitel Building, 1501 Second Avenue (Quasi-judicial).

Date Filed with City Clerk:20100623

City of Seattle
Legislative Department
Office of the City Clerk

Monica Martinez Simmons, City Clerk

January 31, 2011

PARTIES OF RECORD

Dear Sir or Madam:

The City Council at its meeting on January 31, 2011, adopted the recommendation of its Committee on the Built Environment on Clerk File 310914, entitled:

> Appeal of 1507 Group, L.L.C. of a recommendation by the Hearing Examiner on landmark controls and incentives for the Eitel Building, 1501 Second Avenue (Quasi-judicial).

The Committee recommendation was as follows:

> That the Appeal be denied, and affirm the Hearing Examiner recommendation's on controls and incentives for the Eitel Building.

Judicial review of this decision may be sought in King County Superior Court under the Land Use Petition Act (RCW 36.70C). To be timely, an appeal must be filed with the court and served on all parties of record within 21 days of the date the decision is issued. The date of issuance is the date the City Council denied the appeal in Clerk File 310914 (January 31, 2011). For further information please see RCW 36.70C.040

Sincerely,

Monica Martinez Simmons
City Clerk

Enclosure

cc: Sally Clark, Councilmember
Ketil Freeman, Council Central Staff
Karen Gordon, Historic Preservation Officer
Hearing Examiner
Parties of Record

FINDINGS, CONCLUSIONS AND DECISION
OF THE CITY COUNCIL OF THE CITY OF SEATTLE

In the Matter of the Appeal by 1507 Group, L.L.C., From a Recommendation by the City Hearing Examiner the Imposition of Controls and Incentives on the Landmark Eitel Building.	)	C.F. 310914 FINDINGS, CONCLUSIONS AND DECISION

Introduction

This matter involves the appeal by 1507 Group L.L.C. (Owner) from the Hearing Examiner's recommendation for controls and incentive for the Eitel Building (Building), which is located at the northwest corner of the intersection of Pike Street and Second Avenue. The seven-story Building was purchased by the Owner in 1975. In August 2006, the Landmarks Preservation Board (Board) designated the Building as a landmark based on the designation criterion that it "embodies the distinctive visual characteristics of an architectural style, period, or of a method of construction." The Building was nominated for designation by Historic Seattle. In January 2010, the Board recommended controls and incentives. In February 2010, the Owner filed a timely objection to the Board's recommended controls and incentives. The Hearing Examiner conducted a hearing on April 13, 14, and 15 and briefly reconvened on May 12, 2010. On June 9, 2010, the Hearing Examiner recommended that the Council accept the Board's recommendation. On June 23, 2010, the Owner filed an appeal from the Hearing Examiner's recommendation with the City Council. On December 8, 2010, Council's Committee on the Built Environment heard oral argument from the Owner and the Board. On January 12, 2011, the Committee on the Built Environment recommended that the Council deny the appeal by the Owner and affirm the recommendation of the Hearing Examiner.

Findings of Fact

The Council, after considering the record before the Hearing Examiner, hereby adopts the Hearing Examiner's Findings of Fact as stated in the Findings and Recommendation of the Hearing Examiner dated June 9, 2010, a copy of which is attached.

Conclusions

The Council hereby adopts the Hearing Examiner's Conclusions as stated in the Findings and Recommendation of the Hearing Examiner dated June 9, 2010.

Decision

The Council denies the appeal by the Owner and affirms the Hearing Examiner's recommendation that the Council accept the Board's recommended controls and incentives for the Building.

Dated this 31st day of January 2011

City Council President

FINDINGS AND RECOMMENDATION
OF THE HEARING EXAMINER FOR THE CITY OF SEATTLE

In the Matter of Controls and Incentives for

THE EITEL BUILDING
1501 Second Avenue

Hearing Examiner File:
LP-10-001

Board File:
22/10

Introduction

The Landmarks Preservation Board issued a recommendation on controls and incentives for the Eitel Building, located at 1501 Second Avenue, and the property owner timely filed an objection to the recommendation. The matter was heard before the Hearing Examiner on April 13, 14, and 15, and May 12, 2010. Parties represented at the hearing were the property owner, 1507 Group LLC (Owner), by Lawrence A. Costich and Curtis R. Smelser, attorneys-at-law; and the Landmarks Preservation Board (Board), by Roger D. Wynne, Assistant City Attorney. The Examiner visited the property, and the record was held open through May 28, 2010 for post-hearing filings.

For purposes of this recommendation, all section numbers refer to the Seattle Municipal Code, as amended, (SMC or Code) unless otherwise indicated. Having considered the evidence in the record and inspected the site, the Examiner enters the following findings of fact, conclusions and recommendation on controls and incentives.

Findings of Fact

1. The subject property is known as the Eitel Building (building) and is addressed as 1501 Second Avenue. It is located on the northwest corner of the intersection of Second Avenue and Pike Street, within the central business district and two blocks east of the Pike Place Market. It abuts the 38-story Opus condominium tower on the north and is bordered on the west by an alley that runs parallel to Second Avenue. Across the alley is the two-story Liberty Building.

2. The building is a seven-story rectangular structure with tan-colored brick cladding and terra-cotta ornamentation. Six stories were built in 1904 of unreinforced masonry with a steel column and lintel base support system on the southern and eastern sides, and an interior steel column and girder system supporting wood floor and roof framing. The seventh story was added in 1906. The southern and eastern façades are considered primary. Exhibit 26.

3. The building covers most of the 5,592-square-foot site and is approximately 90 feet tall. The basement extends partially under the adjoining sidewalk, and there is a light well that begins with the second floor on the western elevation.

4. The Owner purchased the building in 1975 as an investment in the hope that future renovation would be possible. When renovation to building code standards proved too costly, the Owner rented out the ground floor to commercial tenants and has kept the upper six floors vacant. The Owner also leases out billboard space on the west exterior of the building. Over the years, deterioration and earthquake damage have required structural work to stabilize the building.

5. Until recently, the zoning on the property was DMC (Downtown Mixed Commercial) 240, which would have allowed construction of a 240-foot building. However, in 2004, the Owner obtained a permit to renovate the building within the existing shell. Although the renovations proved too costly for the Owner to proceed, the building permit has been repeatedly renewed and remains active.

6. In 2006, the Owner learned that the property would be rezoned to its present zoning, DMC 240/290-400. The Owner determined that the new zoning would allow one property on the block to be developed to a height of 400 feet but would limit other development on the same block to a maximum height of 160 feet. The Opus tower to the north was to be constructed to approximately 400 feet. Therefore, the Owner decided to construct a 240-foot building on the subject property before the new zoning took effect.

7. The Owner hired an architect, who developed plans for a 22-story building with 92 residential units above 23,000 square feet of administrative office space and 3000 square feet of retail space. The proposal, which included demolition of the existing building, was reviewed in a meeting with the Design Review Board in February of 2006. Exhibit 18.

8. In August of 2006, the Landmarks Preservation Board (Board) designated the building as a landmark following nomination by Historic Seattle. The Board determined that the building "embodies the distinctive visible characteristics of an architectural style, period, or of a method of construction." *See* "Staff's Recommendation on Controls and Incentives" (January 13, 2010) attached to January 26, 2010 letter from Karen Gordon to the Hearing Examiner (Staff's Recommendation). The Owner then retained counsel to negotiate with the Board on a Controls and Incentives Agreement for the building.

9. Following designation, the Owner revised the development proposal for the site to remove the seventh floor and add a 16-story tower above the existing six-story building, preserving the south and east façades. The building would be 16 floors of residential above one level of retail use and five floors of office use. *See* Exhibit 29. The Design Review Board met to consider the revised proposal in October of 2006. Exhibit 19.

10. In January of 2007, the Owner filed a Master Use Permit (MUP) application, thereby vesting to the then-existing 240-foot zoning. At the same time, the Owner submitted the MUP drawings and a project description to the Board's staff and asked to schedule a meeting with the Board's Architectural Review Committee (ARC). Exhibit 27.

11. The ARC is a subcommittee of the Board composed of members with architectural expertise. The ARC is available to meet with an owner to review a proposal, and provide feedback and suggestions on it, before the owner seeks a Certificate of approval from the full Board. The process is collaborative, and the goal is to achieve a design solution that meets both the owner's needs and the Board's goal of preserving the designated historic features. Testimony of Sarah Sodt, 4/15/10 at 1:22. *See* SMC 25.12.750 (reproduced below).

12. A certificate of approval is required from the Board before the owner of a designated landmark may alter or significantly change the designated features or characteristics of the landmark. *See* SMC 25.12.080, .670.

13. The Board's coordinator testified that the Board has granted certificates of approval that resulted in the destruction of some designated features of landmark buildings when the aspects of the buildings that remained were sufficient to convey their historical importance. The coordinator cited two recent examples: the Pacific McKay Ford Building on Westlake Avenue, where the primary façades were removed and are in storage for future installation on a new development; and the Terminal Sales Annex Building at 1931 Second Avenue, a narrow building for which the Board approved retention of the street-facing façade and the addition of a multi-story tower atop the landmark. Testimony of Sarah Sodt, 4/15/10 at 1:22-1:26 and 2:20. She did not know of any certificate of approval application for construction of additional stories atop a landmark that has been denied. Testimony of Sarah Sodt, 4/15/10 at 2:22.

14. It is not necessary for controls and incentives for a building to be in place before an owner seeks a certificate of approval for proposed changes to it. Testimony of Sarah Sodt, 4/15/10 at 1:18.

15. Working with an architect not known to have experience with historical structures, the Owner presented the MUP proposal to the ARC in March of 2007. The ARC suggested that the architect consider an alternative that reduced the tower height and explore a tower setback. The ARC did not state that the design needed to stay within the existing shell of the building. Testimony of Sarah Sodt, 4/15/10 at 1:28-130.

16. To determine the economic impact that might result from controls and incentives that could be adopted for the building, the Owner retained an appraiser to evaluate the feasibility of three development scenarios. The first appraisal was produced on June 8, 2007. The three development scenarios evaluated were office and retail, residential condominium and retail, and residential apartment and retail. They were based on the renovation plans developed for the 2004 building permit. Thus, for each scenario, the appraiser assumed that forthcoming controls and incentives for the building would limit construction to the building's existing shell. *See* Tab 2 to Exhibit 1[1] at 211, 279, 289 and

[1] Tab 2 to Exhibit 1 consists of bound documents, the content of which is essentially the same as the compact disc included under Tab 2 of Exhibit 1. The page numbers referenced in Exhibit 1 and Tab 2 to Exhibit 1 are the Bates-stamped numbers at the bottom of the pages.

299. The appraiser concluded that none of the three development scenarios would be "expected to produce a sufficient return on investment necessary to attract capital to the project." Tab 2 to Exhibit 1 at 193.

17. Under the caption, "Extraordinary Assumptions and Limiting Conditions," the 2007 appraisal notes that the three development scenarios considered "are believed to reflect reasonable and realistic use constraints" that may be imposed on the property through the controls and incentives process. The appraiser reserves the right to modify the appraisal's conclusions if "any or all of the ... assumptions utilized prove to be in error." Tab 2 to Exhibit 1 at 211.

18. The Owner chose not to return to the ARC with a revised design proposal and, instead, filed an application for a certificate of approval in October for essentially the same proposal the ARC had reviewed in March. Exhibits 28 and 29. On November 5, 2007, the Board's staff sent the Owner an application checklist showing which pieces of the certificate of approval application were still missing.

19. On November 15, 2007, as part of the MUP process, the Director of the Department of Planning and Development (DPD) issued a SEPA determination of significance, requiring that an environmental impact statement be prepared to analyze the proposal's historic preservation and land use impacts. Exhibit 22. The Owner retained an environmental consultant to begin work on the EIS. Testimony of Richard Nimmer, 4/13/10 at 10:33.

20. On May 7, 2008, the Owner's appraiser issued an updated appraisal to evaluate the likely economic impact of controls that might be imposed on the building. Tab 2 to Exhibit 1 at 144. Again, the appraisal assumed that any of the three development scenarios would involve "essentially 'rebuilding' the existing seven-story improvement and, in addition, foregoing the opportunity to develop the site to the full extent of the remaining 15 stories." Tab 2 to Exhibit 1 at 172. Under these assumptions, the appraiser again concluded that none of the three scenarios would be capable of producing a sufficient return on investment to attract capital. Tab 2 to Exhibit 1 at 172.

21. The 2008 appraisal also considered the feasibility of the 22-story revised MUP proposal, including demolition of the building, for residential condominium use and residential apartment use. Assuming a minimum rate of return required to attract capital of 75 percent, the appraisal concluded that both of these development scenarios would be feasible. *See* Tab 2 to Exhibit 1 at 169, and 174-76.

22. The Owner believes that as a result of the landmark designation, the building is capped at 90 feet with the exception of a possible small "penthouse" addition. Testimony of Richard Nimmer, 4/13/10 at 10:30. However, the Owner acknowledged that if controls on the building did not prevent an increase in building height, the air rights above the building would be valuable to the owners of adjacent buildings. As an alternative to a tower atop the existing building, the Owner agreed that the air rights could be sold to help fund renovation of the existing building. Testimony of Richard

Nimmer, 4/13/10 at 11:18. The Owner's appraiser agreed that a purchase of air rights could make building renovation possible. Testimony of Brian O'Connor, 4/14/10 at 11:54.

23. On May 9, 2008, the Owner submitted the 2007 and 2008 appraisals to the Board, together with a letter from the Owner's architect, indicating that the application now included demolition of the building, and other materials required to complete the October 2007 certificate of approval application. Exhibit 31.

24. On April 22, 2009, the Owner inquired of DPD concerning the ramifications of placing the revised MUP application on hold while continuing to pursue a certificate of approval from the Board. DPD responded on May 8, 2009, that the Owner would need to terminate the certificate of approval process in order to remove the MUP from active status. Exhibit 24.

25. On May 14, 2009, the Owner notified the Board that it was withdrawing its application for a certificate of approval to demolish the building. Exhibit 25.

26. The Owner and Board continued to discuss controls and incentives for the building. On January 12, 2010, the Owner declared that the negotiations were at an impasse.

27. On January 20, 2010, the Board adopted recommended controls and incentives, which were forwarded to the Hearing Examiner on January 26, 2010. The recommended controls and incentives require that the Owner obtain a certificate of approval from the Board before making alterations or significant changes to the exterior of the building with the exception of the light well on the western elevation. *See* Staff's Recommendation.

28. The Owner timely filed a statement of objections to the Board's recommended controls and incentives. The objections state that the recommended controls are not supported by applicable law and substantial evidence in the record; prevent the owner from realizing a reasonable return on the site; resulted from consideration of factors other than, and in addition to the factors listed in SMC 25.12.590 for determining a reasonable return on the site; deprive the owner of a reasonable economic use of the site; and deny the Owner substantive due process and amount to an inverse condemnation (taking) of the site, in violation of the constitution.

29. In preparation for the hearing on the Owner's objections to the Board's recommended controls and incentives, the Owner's appraiser issued a March 30, 2010 summary appraisal of the property that updated information on its market value. Exhibit 1, Tab 11 at 489. The appraiser determined that the "highest and best use" of the property was to "hold for future development" and valued it at $2,500,000 under the "vested MUP" proposal, and $1,650,000 under the existing 160-foot zoning assuming that no controls were imposed. Exhibit 1, Tab 11 at 493, 582 and 587.

30. On April 7, 2010, the Owner's appraiser issued an updated appraisal to evaluate the economic impact of the imposition of controls on the property. Exhibit 1, Tab 12 at 603.

The appraiser again assumed that the Owner would be required to preserve the existing shell of the building other than the light well. Exhibit 1, Tab 12 at 626. And the appraiser again reserved the right to modify the conclusions in the report should the assumption on controls be proven incorrect. Exhibit 1, Tab 12 at 626. As in the earlier appraisals, the appraiser concluded that "rehabilitation of the existing improvements is not considered to be feasible" under the assumed controls. Exhibit 1, Tab 12 at 605.

Applicable Law

31. SMC 25.12.570 provides that "[o] n the basis of all the evidence presented at hearing," the Examiner is to determine whether to recommend that the proposed controls and incentives recommended by the Board be accepted, rejected or modified. Further, the Examiner "shall not recommend any control which is inconsistent with any provision of this chapter, or which requires that the ... [landmark] be devoted to a particular use," or that imposes any use restriction, control or incentive if the effect, alone or in combination, "would be to prevent the owner from realizing a reasonable return on the [landmark]." SMC 25.12.590 lists the factors to be considered in determining a reasonable return on the landmark.

32. SMC 25.12.580 states that "in no event shall ... any proceedings under or application of this chapter deprive any owner of a ... [landmark] of a reasonable economic use of such ... [landmark]."

33. SMC 25.12.750 lists the factors that the Board and Examiner are to take into account in considering an application for a certificate of approval. The factors relevant to this case are the following:

> A. The extent to which the proposed alteration or significant change would adversely affect the specific ... [landmarked] features or characteristics...;
>
> B: The reasonableness or lack thereof of the proposed alteration or significant change in light of other alternatives available to achieve the objectives of the owner and the applicant;
>
> C. The extent to which the proposed alteration or significant change may be necessary to meet the requirements of any other state law, statute, regulation, code or ordinance; [and]
>
> D. Where the Hearing Examiner has made a decision on controls and economic incentives, the extent to which the proposed alteration or significant change is necessary or appropriate to achieving for the owner or applicant a reasonable return on the ... [landmark], taking into consideration the factors specified in Sections 25.12.570 through 25.12.600 and the economic consequences of denial; provided that, in considering the factors specified in Section 25.12.590 for purpose of this subsection, reference to the times before or after the imposition of controls

shall be deemed to apply to times before or after the grant or denial of a certificate of approval;

....

Conclusions

1. The Hearing Examiner has jurisdiction over this matter pursuant to SMC 25.12.540.

2. The Owner's constitutional issues of inverse condemnation and substantive due process are beyond the jurisdiction of a quasi-judicial body, and the Examiner has not considered them. *See Yakima Cy. Clean Air Authority v. Glascam Builders, Inc.*, 85 Wn.2d 255, 257, 534 P.2d 33 (1975).

3. Under the scheme of Subchapter V. of Chapter 25.12 SMC, the Hearing Examiner's recommendation on controls and incentives is essentially *de novo*. The issue before the Examiner under SMC 25.12.560.B is whether the Board's recommended controls and incentives are supported by substantial evidence in the record before the Examiner. "Under the substantial evidence standard, there must be a sufficient quantum of evidence in the record to persuade a reasonable person that the declared premise is true." *Wenatchee Sportsmen Ass'n v. Chelan Cy.*141 Wn.2d 169, 176, 4 P.3d 123 (2000) (citations omitted). The "appellant bears the burden of proving that the Board's recommendation should be rejected or modified." SMC 25.12.560.B. The "appellant" in this case is the Owner.

4. The Owner objects to the Board's recommendation as not being supported by applicable law and substantial evidence in the record before the Board. As noted, however, the Examiner's review under the Code is *de novo*. Therefore, the record before the Board is immaterial in this proceeding.

5. The Owner asserts that the Board erroneously considered factors other than, and in addition to the exclusive factors listed in SMC 25.12.590 for determining a reasonable return on the site. However, the Owner did not establish what factors the Board considered in reaching its recommendation on controls and incentives. Moreover, the issue before the Examiner is not what the Board considered but whether the Board's recommended controls and incentives are supported by substantial evidence in the record before the Examiner.

6. The Owner's entire case, including all the work of the Owner's appraiser, rests on the premise that the Board's recommended controls would limit any development of the property to the shell of the existing building. Yet there is no evidence in record to support that premise.

7. The recommended controls require only that the Owner obtain a certificate of approval from the Board before making exterior alterations to the building, with the exception of eliminating the light well. Both the evidence in the record and the

applicable law demonstrate that the certificate of approval process is a collaborative one, designed to achieve both the owner's and City's needs with respect to the landmark.

8. The Owner argues that the addition of floors to the building would "significantly change and adversely affect" the features or characteristics specified in the designation, and that it is not clear the Board would approve such a change. However, the certificate of approval process exists to examine and, if possible, resolve such challenges. The ARC works with the owner toward development of alternative designs. The Board considers several factors, including the reasonableness of the proposed alteration in light of the alternatives available to achieve the owner's objectives. *See* SMC 25.12.750.B (Finding 33). The Code does not dictate a particular outcome, nor does it require preservation of all designated historic features. Moreover, past Board practice, including this Owner's experience with the ARC, demonstrates that approval of a tower above the landmark is in no way foreclosed.

9. The Owner states that if the Board had believed additional height was acceptable, it would have said so in its recommendation, as it did with the exception allowing infill of the light well. The Board is not a legislative body, and it is not clear that the rules of statutory construction apply to its recommendation. In any event, the fact that the Board did not include an exception for additional height above the landmark does not indicate that additional height is precluded; rather, it suggests that the addition of floors above the landmark would require the exploration of alternatives that is an inherent part of the certificate of approval process.

10. The Owner correctly asserts that the evidence fails to demonstrate that adding floors to the building could be accomplished and would provide the Owner a reasonable rate of return. The evidence does show that from 2006 through 2007, the Owner pursued the original 22-story MUP proposal that included preservation of the south and east façades and construction of a tower above the existing landmark. Working with an architect not known to have experience with historical structures, the Owner met with the Design Review Board and the ARC on the MUP proposal. Both bodies asked for revised alternatives, although for slightly different reasons. The evidence shows that in 2008, the Owner received an appraisal that indicated demolition of the landmark and sale of the property for construction of a 240-foot or 160-foot tower would result in a rate of return necessary to attract capital to the project. The evidence also shows that in 2008, the Owner decided to demolish the building and terminated the certificate of approval process. During the intervening two years, the Owner has directed resources toward convincing the Board that any controls and incentives placed on the landmark would prevent the Owner from realizing a reasonable return and deprive the Owner of a reasonable economic use. As a result, we do not know with certainty whether a tower can be built atop the landmark, and there is no evidence in the record on whether development available to the Owner through the MUP and certificate of approval processes would provide the Owner with a reasonable return and a reasonable economic use. The Board's recommended controls and incentives would afford the opportunity for development of the information necessary to make those determinations. *See* SMC 25.12.750.D (Finding 33).

11. The Owner drew an analogy between this case and In re Bon Marche Stables, LP-08-004, which also involved an owner's challenge to the imposition of controls and incentives that required a certificate of approval for exterior alterations. In that case, however, the Board did not dispute that the imposition of controls and incentives would limit future development to the shell of the existing building.

12. Because all of the Owner's evidence is based on an invalid assumption, the Owner has not met the burden of proving that the Board's recommended controls and incentives should be rejected or modified.

Recommendation

The Hearing Examiner recommends that the City Council accept the Board's recommendation on controls and incentives for the Eitel Building.

Entered this 9th day of June, 2010.

Sue A. Tanner
Hearing Examiner

Concerning Further Review

NOTE: It is the responsibility of the person seeking further review of a Hearing Examiner recommendation to consult appropriate Code sections to determine applicable rights and responsibilities.

SMC 25.12.620 provides as follows:

> Any party of record before the Hearing Examiner may appeal the recommendations of the Hearing Examiner regarding controls and incentives to the Council by filing with the City Clerk and serving on all other parties of record a written notice of appeal within fourteen (14) days after the Hearing Examiner's decision is served on the party appealing.

BEFORE THE CITY COUNCIL

OF THE CITY OF SEATTLE

In the Matter of Controls and Incentives for **THE EITEL BUILDING** **1501 Second Avenue**	Hearing Examiner File: **LP-10-001** Landmark Preservation Board File: **22/10** **1507 GROUP'S APPEAL OF HEARING EXAMINER'S RECOMMENDATION**

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II. RELIEF REQUESTED

1507 Group LLC (the "Owner") brings this appeal to the Seattle City Council, in accordance with the provisions of Seattle Municipal Code ("SMC") 25.12.054, to state its objections to the Hearing Examiner's Findings and Recommendations, entered June 9, 2010, and to correct the substantive errors regarding the controls and incentives imposed on 1501 Second Avenue (the "Eitel Building").

III. INTRODUCTION AND SUMMARY

The Eitel Building is located on the corner of Second Avenue and Pike Street in the heart of downtown Seattle. (Hearing Examiner's Findings and Recommendations ("F.R. p.1, ¶1).) The Owner purchased the building as an investment in 1975. (F.R. p.1, ¶1.) The 2001 Nisqually earthquake caused substantial damage to The Eitel Building and, as a result, it is currently underutilized. *Id.* The Owner leases the ground level to a wig shop, a nail parlor, a shoe store and a teriyaki restaurant, but the remaining six stories are vacant awaiting redevelopment. **Exhibit 3**. Seeking to further the development occurring in the neighborhood and obtain an economic return on the building, the Owner applied for a Master Use Permit ("MUP") for redevelopment of the property. (F.R. p.2,

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¶10.) In apparent response to these redevelopment plans, the adjoining property owners retained the Johnson Partnership, a Seattle architectural firm, to nominate The Eitel Building as a landmark and prevent the Owner from taking advantage of the available development heights—as such would impact views.

On August 2, 2006, the Landmark Preservation Board (the "Board") voted to designate the Eitel Building as a Seattle Landmark based on only one designation criterion, SMC 25.12.350(D): "It embodies the distinctive visible characteristics of an architectural style, period or of a method of construction." The approval of designation was strongly opposed by the Owner. Nevertheless, once designated, the Owner fully cooperated with the Board's staff to negotiate the controls and incentives agreement as provided by SMC 25.12.490. What ensued next was more than three years of effort by the Owner in a vain attempt to meet the Staff's ever changing and vague comments on the documents and feasibility studies commissioned by the Owner. *See* **Exhibit 33, p. 11**. The Owner has sought to find a way to make the building provide an economically reasonable return. Absent the ability to utilize the additional height limitations available in the zoning for the Eitel Building, remodeling for occupation the other six floors of the building (that currently lay vacant) is economically unfeasible.[1] *See* **Exhibit 33, p. 11.**

IV. BOARD CONTROLS AND INCENTIVES RECOMMENDATION

When the Board designates a building as a landmark, Board staff members are directed by the SMC to negotiate with the landmark owner to determine what controls and incentives should be placed on the building. *See* SMC 25.12.490. 'Controls' are specific restrictions imposed by ordinance to prevent alternating or changing landmarks. SMC

[1] The Owner spent considerable time and financial resources on this negotiation effort, including: economic consultant/appraisal services by the O'Connor Consulting Group; historic preservation consultation with Kovalenko Hale Architects; preservation and redevelopment cost estimates by W.G. Clark Construction and Matson Carlson & Associates; structural engineering by Coughlin Porter Lundeen; and legal services of Schwabe, Williams & Wyatt for application of the Landmark ordinance. The Owner's efforts to negotiate the controls and incentives agreement resulted in a substantial collection of analyses prepared by the Owner's team of professionals. No professionals were retained by the Board.

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25.12.090. The present appeal to the City Council challenges the process by which the controls were recommended and the validity of these recommended controls under the SMC.

The Owner, concerned that the controls would prevent an economic use of the building, hired a number of experts to look at the options for the building. The experts originally concluded that ". . . in the absence of appropriately supportive incentives, the required preservation and renovations of the subject property through controls and incentives simply cannot help but lead to a devastating financial and economic impact on an owner. Such an outcome is specifically prohibited by SMC 25.12.580." **Exhibit 1, Tab 2** (EITEL 00039). After negotiations began with the Board, these opinions were reviewed.

> Rehabilitation and preservation of the Eitel Building under the relevant scenarios will result in financial loss, even when applying all available incentives. Given this result, a rate of return necessary to attract capital investment cannot reasonably be attained. Because of its age and condition, the costs associated with rehabilitating the Eitel Building are expected to be inordinately high, particularly when considering the seismic retrofitting necessary to make the building habitable. In fact, the recently updated cost estimates provided by a second independent estimator, indicates that construction costs to be approximately $3 million higher than those costs used for the [O'Connor Consulting Group] appraisal.

Exhibit 1, Tab 2 (EITEL 00057) (underline added).

In May 2009, the Owner's real estate appraiser, O'Connor Consulting Group, concluded that the property's market value was as high as $3.645 million if no controls were imposed on the Eitel Building. **Exhibit 1, Tab 2** (EITEL 00055). But, given the disproportionately high construction costs for preservation of the Eitel Building, the property's market value was reduced to less than zero under all preservation scenarios. *Id.* Controls that would prevent the Owner from building to the allowed height level would make any redevelopment or improvements to the building economically infeasible. *Id.*

Controls recommended by the Board must: 1) Relate to the specific feature or features of the site/improvements in the designation report; 2) Set forth the reasons for the

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proposed controls and incentives; and 3) State the circumstances that would require the Owner to obtain a certificate of approval before altering or changing the site/improvement if the controls are imposed. SMC 25.12.520. The Board, without providing any real explanation, rejected the Owner's concerns and recommended controls that prevent any alteration to the exterior of the building.[2]

Specifically the Board provided the following:

> A Certificate of Approval, issued by the City of Seattle's Landmarks Preservation Board pursuant to Seattle Municipal Code ("SMC"), Ch. 25.12, must be obtained, or the time for denying a Certificate of Approval application must have expired, before the owner of the landmark . . . may make alterations or significant changes to: The exterior of the building, provided that the Certificate of Approval requirement shall not preclude elimination of the light well on the west elevation.

Exhibit 1, Tab 1 (EITEL 00743) (Staff Recommendation on Controls and Incentives). A "certificate of approval" is a written authorization that must be issued by the Board before any alteration or significant change may be made to a feature upon which an ordinance has been passed establishing a control. SMC 25.12.080.

The Owner objected to the control requiring a "certificate of approval" for the whole exterior—the basis of the designation under SMC 25.12.350(D) implies that only alterations to the façade were restricted. The overly-broad restriction imposed by the Board's control effectively prevents the Owner from building above the Eitel Building's existing height to its perimeter, which would be necessary achieve a viable economic return.[3] The Owner also

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[2] As demonstrated throughout the hearing on this matter and acknowledged by the City of Seattle Assistant Prosecuting Attorney and the Board's witnesses, the Board has routinely ignored the provisions of the Seattle Municipal Code for determining whether controls may be imposed on the Eitel Building. The Board provided no substantive written review of the numerous appraisal, cost estimates and expert reports furnished by the Owner prior to making its recommendation to impose controls. Since making its Recommendation on Controls and Incentives, the Board continued to ignore the Code requirements, instead relying on speculative conclusions by its witnesses that have no bearing on the exclusive factors identified under SMC 25.12.590. *Discussed below.*

[3] In October, 2007, the Owner applied for a certificate of approval to building a tower above the existing structure while preserving its façade. *See* **Exhibit 28.** As the Owner testified to the Hearing Examiner, the Board's Architectural Control Committee sought changes to the proposed design that would set the tower back

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challenged the imposition of any controls, since rehabilitating the building is prohibitively expensive. A hearing occurred before Hearing Examiner Sue A. Tanner in April and May of 2010.

V. CONTROLS AND INCENTIVES HEARING

During a "controls" hearing, the Hearing Examiner must determine whether to recommend, accept, reject, or modify any or all of the proposed controls and incentives, but the hearing examiner is explicitly forbidden from recommending any control inconsistent with the SMC or "any control or incentive if the effect of such control, incentive or combination thereof would be to prevent the owner from realizing a reasonable return on the site, improvement, or object." SMC 25.12.570. The concern about depriving a property owner of a reasonable return is echoed in SMC 25.12.580, which explicitly provides that "[i]n no event shall the recommendation of the Hearing Examiner or any proceedings under or application of this chapter deprive any owner of a site, improvement or object of a reasonable economic use of such site, improvement or object."

The Owner requested the hearing because credible evidence demonstrated that the controls would prevent the Owner from realizing an economic return and that the Board's recommendation was made without considering the elements in the SMC that govern when a control is inappropriate due to economic reasons and without consulting any experts. The Hearing Examiner adopted the recommendation made by the Board, stating:

> The recommended controls require only that the Owner obtain a certificate of approval from the Board before making exterior alterations to the building, with the exception of eliminating the light well. Both the evidence in the record and the applicable law demonstrate that the certificate of approval process is a collaborative one, designed to achieve both the owner's and City's needs with respect to the landmark.

Findings and Recommendation of the Hearing Examiner, Conclusion no. 7.

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from the perimeter of the structure, effectively rendering such an addition as infeasible.

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The Owner appeals now to the Seattle City Council because it believes the Board and the Hearing Examiner are misreading the code and confuse controls and incentives with certificates of approval. By doing so, they have made recommendations imposing controls that are improper under the SMC and render the controls and incentives process as meaningless. The Owner also appeals because the incorrect burden and standard of review were imposed, improper testimony was allowed, and there is clear evidence that controls on the Eitel Building would prevent the Owner from realizing a reasonable return and would deprive the Owner of reasonable economic use of The Eitel Building.[4]

VI. STATEMENT OF ERRORS BY THE HEARING EXAMINER

The Owner challenged the controls placed upon The Eitel Building resulting in the decision from which they now appeal. The Owner requests that the Seattle City Council, in its quasi-judicial function, overturn the Hearing Examiner's decision and/or remove the controls on The Eitel Building because of the following errors:

1. The Hearing Examiner failed to apply the correct standard of review required by 25.12.560(b);
    - The Hearing Examiner stated that she had *de novo* review, or rather, the ability to review the matter anew. She did not under SMC 25.12.560(b) (Conclusion Nos. 3- 5; Applicable Law 31);
    - The Hearing Examiner failed to acknowledge that the Board was required to show that its recommendation was made based on the applicable law and substantial evidence (Conclusion No. 4 and No. 5);
    - The Hearing Examiner did not acknowledge the shifting burdens created by SMC 25.12.560 (Conclusion No. 4, No. 5, No. 12; Applicable Law 31).
2. The Hearing Examiner relied on the wrong standards and based her decision upon the standards for a certificate of approval under SMC 25.12.750 (Conclusion No. 7, No. 8, No. 11; Applicable Law 33);

[4] To the extent the City Council interprets that the element to be preserved under the Eitel Building's landmark designation is its façade and that the controls imposed do not require a certificate of approval for any additions above the existing building height, the City Council can modify the Hearing Examiner's recommendation on controls and incentives accordingly. Thus, the Owner would be free to additional development above the structure and no certificate of approval would be needed to do so.

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3. The Hearing Examiner's Recommendations on proposed controls were unsupported under applicable law and/or substantial evidence in the record in violation of SMC 25.12.560 (Conclusion Nos. 6–12);

- The Hearing Examiner's Recommendations prevent the Owner from realizing a reasonable return on The Eitel Building in violation of SMC 25.12.570 and SMC 25.12.590;
- The Hearing Examiner's Recommendations also deprive the Owner of reasonable economic use of The Eitel Building;

4. The Hearing Examiner upheld recommendations made by the Landmark Preservation Board that were obtained in the absence of any collaboration with the Owner, despite months of the Owner's attempts to open a dialogue about the building (Conclusion Nos. 5-7).

VII. STANDARD OF REVIEW

Pursuant to SMC 25.12.630, the City Council may reject or modify the Hearing Examiner's recommendations on controls & incentives if the Owner carries its burden of establishing that one of the following standards are met:

(a) The Hearing Examiner's recommendation is not supported by substantial evidence when viewed in light of the record before the Council; and

(b) The Hearing Examiner's recommendation is not supported by applicable law.

A substantial evidence challenge requires the reviewing body to ask whether there is "sufficient quantum of evidence in the record to persuade a reasonable person that the declared premise is true." *Wenatchee Sportsmen Ass'n v. Chelan County*, 141 Wn.2d 169, 176, 4 P.3d 123 (2000). If this standard is not met or if the City Council concludes that the Hearing Examiner did not follow the law and municipal code, the City Council must reject or modify the recommendations on controls and incentives. SMC 25.12.630; *see Sleasman v. City of Lacey,* 159 Wn.2d 639, 646, 151 Wn.2d 639 (2007) (holding that an incorrect application of law is reversible error). Neither the Hearing Examiner nor the Board's recommendations are entitled to deference.

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As set forth in this brief, the Owner challenges the following Conclusions of the Hearing Examiners because they were unsupported by either substantial evidence and / or the applicable law: Conclusion Nos. 3–12; and Findings of Applicable Law Nos. 31 and 33.

VIII. ARGUMENT AND AUTHORITIES

The Hearing Examiner's decision violates the basic tenants of review under the SMC for controls and incentive agreements: the recommendations of the Hearing Examiner deprive the owner of reasonable economic use of the Eitel Building. This, however, is not the only consequence associated with upholding the recommendations.

The way in which the Board and the Hearing Examiner interpret the SMC is illogical and inconsistent with the spirit of the landmarks preservation code. The Owner was held to the wrong standards and burdens throughout these proceedings. The Owner provided uncontroverted evidence on appraisal and economic impact resulting from imposition of the controls and incentives only to have the Board ignore this economic analysis and proceed with a recommendation that contradicted the code's mandate. The Hearing Examiner compounded this error by ignoring the unambiguous language in the code and applying factors found in another subchapter of the SMC.

The City Council is asked to rectify this error of law. By overturning the Hearing Examiner's Recommendation, the City Council can cure a fundamental injustice with the way in which controls and incentives were reviewed in this case.

A. The Hearing Examiner Misapplied The Standard of Review in SMC 25.12.560(B).

The Hearing Examiner made a number of errors during the hearing and in the Findings and Recommendations. But the error that most drastically impacts the Owner is the Hearing Examiner's refusal to consider SMC 25.12.560(b)[5] as applicable law. In this regard,

[5] SMC 25.12.560 governs the procedure to be followed by the Hearing Examiner and is explicitly titled "Hearing Examiner procedure."

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the Hearing Examiner's Conclusion No. 4 states:

> The Owner objects to the Board's recommendation as not being supported by applicable law and substantial evidence in the record before the Board. As noted, however, the Examiner's review under the Code is *de novo*. Therefore, the record before the Board is immaterial in this proceeding.

(F.R. p.7, ¶ 4 ("Conclusion 4").)

The SMC requires that the Board's recommendation on proposed controls and incentives "be supported by applicable law and substantial evidence in the record." SMC 25.12.560(b). Here, the Board justified its recommendation on improper factors, did not follow applicable law, and did not have substantial evidence supporting its original recommendation. The Hearing Examiner accepted the recommendation anyway, believing that the code gave the full burden of persuasion to the Owner, and because new evidence appeared that could support the recommendation, the Owner was not entitled to relief. (F.R. p.7, ¶ 3 ("Conclusion 3").) This was a fundamental misreading of the SMC's requirements concerning the standard of review and ignores the shifting burden imposed on the Board to support its recommended controls.

1. The Hearing Examiner's Review Is Not *De Novo*.

The Hearing Examiner erred by concluding her review was *de novo*. "A trial or hearing "*de novo*" means trying the matter anew the same as if it had not been heard before and as if no decision had been previously rendered . . . ." *Matter of Deming*, 108 Wn.2d 82, 88, 736 P.2d 639 (1987) (citing Am.Jur.2d § 698, p. 597 (1962)). "The term de novo means afresh, anew, a second time, and there cannot be a hearing de novo if there has not been an original hearing." *Hoagland v. Mount Vernon School Dist. No. 320, Skagit County*, 95 Wn.2d 424, 432, 623 P.2d 1156 (1981). The Hearing Examiner concluded, "Under the scheme of Subchapter V. of Chapter 25.12 SMC, the Hearing Examiner's recommendation on controls and incentives is essentially *de novo*." (F.R. p.7, ¶ 3 ("Conclusion 3").) This was in error. The Hearing Examiner does not have authority for a *de novo* review for a controls and

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incentive recommendation made by the Board.

SMC 25.12.560 governs the procedure to be followed by the Hearing Examiner and is explicitly titled "Hearing Examiner procedure." It states:

> A. Proceedings before the Hearing Examiner shall be in accordance with the procedures for hearings in contested cases pursuant to the Administrative Code, Chapter 3.02 of the Seattle Municipal Code, and the Hearing Examiner's Rules of Practice and Procedure in effect at the time of the proceeding, except as such procedures are modified by this chapter.
>
> B. The Board's recommendation on proposed controls and incentives must be supported by applicable law and substantial evidence in the record. The appellant bears the burden of proving that the Board's recommendation should be rejected or modified.

SMC 25.12.570 also governs the basis for the hearing examiner's recommendation. It states:

> On the basis of all the evidence presented at a hearing, the Hearing Examiner shall determine whether to recommend, accept, reject or modify all or any of the proposed controls and economic incentives recommended by the Board, and/or whether to recommend a modified version of any of the proposed controls or incentives. The Hearing Examiner shall not recommend any control which is inconsistent with any provision of this chapter, or which requires that the site, improvement or object be devoted to any particular use, or which imposes any use restrictions, or any control or incentive if the effect of such control, incentive or combination thereof would be to prevent the owner from realizing a reasonable return on the site, improvement, or object.

Because the Hearing Examiner procedure created by the SMC requires the Board to present to the Hearing Examiner a recommendation that is supported by applicable law and substantial evidence, the Hearing Examiner may not accept the Board's proposed controls and incentives in the absence of a recommendation by the Board that was made under these conditions. Therefore, the review is not *de novo.*

Ordinances are read as a whole. *City of Spokane v. Carlson*, 96 Wn. App. 279, 883, 979 P.2d 880 (1999); *see also State v. Hughes*, 80 Wn.App. 196, 199, 907 P.2d 336 (1995).

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An unambiguous ordinance will be applied by its plain meaning. *Sleasman*, 159 Wn.2d at 643 (holding that "full effect must be given to the legislature's language, with no part rendered meaningless or superfluous"); *see Carlson*, 96 Wn. App. at 883 (holding that local ordinances are to be read "sensibly to effect the legislative intent and to avoid an unjust and absurd result"). The Hearing Examiner erred by reading SMC 25.12.570 without SMC 25.12.560(b) because doing so is not reading the chapter of ordinances as a whole and creates an unjust and absurd result.

2. The Board Had The Burden To Show Its Recommendation Was Supported By Applicable Law And Substantial Evidence.

"*The record before the Board is immaterial in this proceeding.*" (F.R. p.7, ¶ 4 ("Conclusion 4").) These ten words show the fundamental error in the Hearing Examiner's review. To the extent that the Hearing Examiner considered SMC 25.12.560(b) she did so improperly when she found that the Owner carried the full burden in the hearing, and failed to require the Board to show that the decision it made had been a decision supported by the applicable law and substantial evidence.

Following the Board's argument, she interpreted SMC to mean that the Board must be able to support its decision, at the time of the hearing, by applicable law and substantial evidence. She then determined that, under SMC 25.12.570, she had the power to determine a recommendation *de novo*, or anew. Her conclusions are almost exclusively based on information not before the Board at the time of the recommendation that she was reviewing.

The Owner asserted that this Code requires the Board to apply applicable law and to have had substantial evidence to support its recommendation at the *time* the recommendation was made and to demonstrate this at the hearing. It argued that the Hearing Examiner's recommendation could not be to uphold the recommendation of the Board if the Board did not have substantial evidence and/or did not follow applicable law in coming to its recommendation. In this case, the distinction between these positions makes all the

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difference.[6]

3. The Recommendation Made By The Board Is Without Supporting Evidence.

During the three years in which the Owner attempted to negotiate the controls and incentives agreement, it met with the Board's staff five times and with several members of the Board once. In a letter dated January 7, 2010, the Board's staff rejected the conclusions reached by the Owner's economic consultant—i.e., that imposing preservation controls on the Eitel Building will leave the Owner without an economic use of the building—but failed to provide any substantive comments or bases for its rejection. At that point, it became apparent to the Owner that both the City staff and Board were misinterpreting or misapplying the requirements under SMC 25.12.490 *et seq.* The primary concern was that the Board staff was relying on unavailable or speculative evidence to support its belief that redevelopment was economically feasible. On January 12, 2010, the Owner declared an impasse in the negotiation pursuant to SMC 25.12.520.

The City offered no substantive critique of the Owner's reports and had provided no independent preservation cost estimates, appraisal reports or economic analysis.[7] Indeed, the City staff and members of the Board have challenged the findings of the Owner's professionals with nothing more than unsupported conclusory statements and subjective speculation: they stated, without evidence, that the Owner may be able to get credit for affordable housing.

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[6] The Owner spent years trying to provide information to the Board and the Board's staff about this building, only to have new objections to the controls arise at the time of the hearing that had never been discussed during the negotiation phase or when the Board made its recommendation. Due to the limited discovery and procedure associated with Hearing Examiner review, the Owner was subject to new arguments that the Board admits it never considered at the time of its recommendation. The only argument considered and raised during the Board recommendation was a belief that low income housing tax credits may be available to help redevelopment. The Hearing Examiner did not mention this argument in her Findings and Recommendations.

[7] Noteworthy is the fact that the only written review comments furnished by the Board in response to the Owner's submittals were those found under **Exhibit 1, Tab 2**, (EITEL00030-00053). This document shows the reply to the City's comments by the Owner's expert, Brian O'Connor.

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Before the hearing, the Board had not previously engaged the services of a licensed appraiser to review the appraisal and economic feasibility reports prepared by the Owner's consultant, O'Connor Consulting Group, according to testimony by the coordinator for the Board, Sarah Sodt. Neither the Board members nor its staff have expertise in these highly technical areas.

In spite of these shortcomings, the Board's staff nonetheless recommended controls be imposed on the Eitel Building and did nothing but encourage the Owner to take on more and more expense as the Board asked questions of the experts. On January 20, 2010, the Board considered the Controls put forth by its staff and approved them as recommended. This decision was arbitrary at best.

An act is arbitrary or capricious if it is a "willful and unreasonable action, without consideration and regard for facts or circumstances." *Landmark Dev., Inc. v. City of Roy*, 138 Wn.2d 561, 573, 980 P.2d 1234 (1999) (quoting *Teter v. Clark County*, 104 Wn.2d 227, 237, 704 P.2d 1171 (1985)). A finding of fact made without evidence in the record to support it, and an order based upon such finding, is arbitrary. *Miller v. City of Tacoma*, 61 Wn.2d 374, 390, 378 P.2d 464 (1963)). This principle should be analogized to this situation where a Board has made a recommendation without any facts relating to the applicable law that would support this recommendation. *See Maranatha v. Pierce County*, 59 Wn. App 795, 804, 801 P.2d 985 (1990)(finding arbitrary and capricious conduct by local government when its decision is made "without consideration and in disregard of the facts"). As in *Maranatha*, the Board's recommendation is a textbook example of arbitrary conduct that must be remedied. Ms. Sodt stated at the Controls and Incentives Board Meeting that while a lot of information had been received from the owners, she felt that the information presented did not justify deviating from the "standard" agreement. **Exhibit 33, p. 8.** The imposition of a standard agreement again speaks volumes about the "negotiations" taking place before the landmarks preservation board. *Id.*

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This is not the system contemplated by the "negotiations" discussed in the SMC. Moreover, it is unjust to allow the Board to make unsupported decisions, and then, after the fact, concoct arguments that try to support these. This behavior directly prejudiced the Owner, as shown in Conclusion 10, when the Hearing Examiner punished the Owner for not having an analysis on one scenario—a scenario that appeared for the first time in the closing arguments of the Board. (F.R. p.8, ¶10.) For years, the Owner calculated and recalculated its numbers to respond to vague questions from the Board, only to find a new argument raised by the Board during the hearing.

4. Since The Board Had Undergone No Expert Review, There Was No "Substantial Evidence" To Provide To The Hearing Examiner From The Recommendation Process.

While the term "substantial evidence" has not been defined in the context of SMC 25.12.560(b), the term is frequently used in the land use context, and in other contexts, to mean evidence that would persuade a reasonable person that the declared premise is true. *See e.g. Wenatchee Sportsmen Ass'n v. Chelan Cy.*, 141 Wn.2d 169, 176, 4 P.3d 123 (2000) (land use); *Abbey Rd. Group, LLC v. City of Bonney Lake*, 167 Wn.2d 242, 218 P.3d 180 (2009); *Residents Opposed to Kittitas Turbines v. State Energy Facility Site Evaluation Council*, 165 Wn.2d 275, 197 P.3d 1153 (2008).

In the matter of The Eitel Building, the Board's recommendation was supported by nothing other than a rejection of the evidence submitted by the Owner. It was only at the hearing that the Board sought to support its recommendations, but it did so with speculation. Speculation is not substantial evidence in that it is not evidence that would persuade a reasonable person that a declared premise is correct. *See Hausworth v. Pom-Arleau*, 11 Wn.2d 354, 119 P.2d 674 (1941) (finding that a witness's testimony that is speculative did not constitute substantial evidence); *see also Little v. King*, 160 Wn.2d 696, 705, 161 P.3d 345 (2007). In land use cases, where a Board's decision has been based on speculation,

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appellate courts have found that substantial evidence failed to support the Board's decision. *Robertson v. May*, 153 Wn. App. 57, 94, 218 P.3d 211 (2009). In other types of cases, courts have required testimony to have more than a speculative value before that testimony could sufficiently establish a material fact—it is contrary to assert that such suspect testimony could lay the basis for substantial evidence. *See Pol. v. Seattle*, 200 Wash. 208, 214 (1939) (proposition that speculative value is insufficient to establish material fact).

Here, the Board has defended its recommendations with speculation. The Board's experts testified about the possibility of maybe, one day, obtaining low-income housing tax credits, being helped by future market rates, or unknown future investors willing to enter the project. This speculation does not establish substantial evidence to support the Board's decision. Despite the fact that these Low Income Housing Tax Credits were the primary argument made by the Board during the hearing, and dominated the proceedings, it was a flawed argument: so flawed, in fact, that the Hearing Examiner left it out of her Findings and Recommendations completely.

5. The Hearing Examiner Misunderstood the Shifting Burden Imposed In SMC 25.12.560(b) and Instead Placed All Burden on The Owner.

The SMC requires the Board to support its recommendation with substantial evidence to prevent summary rejections of concerns presented by owners. While the SMC also requires that at the hearing "[t]he appellant bears the burden of proving that the Board's recommendation should be rejected or modified" this burden only arises after the Board has presented a recommendation that has prima facie support. *See* SMC 25.12.560(b).

In other words, SMC 25.12.560(b) creates a shifting burden. After the Board provides substantial evidence supporting its decision, the burden then shifts to the Owner to establish a reason to reject the proposal. As this shifting burden is occurring, it is the Hearing Examiner's duty pursuant to SMC 25.12.570 to determine whether to recommend, accept,

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reject or modify all or any of the proposed controls and economic incentives. . ." as long as no recommendation is made that is "inconsistent with any provision of this chapter . . ." By upholding the recommendation of the Board despite testimony that the Board did not follow the Code, and considered the Low Income Housing Tax Credits (an impermissible factor under SMC 25.12.590), the Hearing Examiner was acting impermissibly. She misunderstood the provisions of SMC 25.12.570 to give her *de novo* review, but failed to take into consideration the procedure established in SMC 25.12.560(b) that required her to review the Board's decision—not the matter anew.

Where the Board failed to show that it applied the applicable law when making its recommendations, and failed to provide substantial evidence supporting its decision to make the recommendations, and where the Hearing Examiner found that it was the burden of the Owner to prove that the Board made its decision without substantial evidence and by using improper factors, the Hearing Examiner erred. She took evidence not available or considered by the Board members when they were making their decision and held the Owner to the wrong standard. As a result, the City Council should overturn the recommendation.

B. The Hearing Examiner Confused the Process for Obtaining a Certificate of Approval with the Process for Determining Controls.

As discussed above, ordinances are read as a whole and are to be construed sensibly to effect the legislative intent and to avoid an unjust and absurd result. *Sleasman,* 159Wn.2d at 646; *Carlson*, 96 Wn. App. at 883; *Hughes*, 80 Wn.App. at 199. The Hearing Examiner also erred by finding SMC 25.12.750 to be applicable law, but not SMC 25.12. 590. As a result, Conclusion No. 7, No. 8, No. 11 and Applicable Law 33 are all in error. The Hearing Examiner's reasoning in these conclusions of law and in the application of law number 33 would render the controls and incentive agreement negotiations as meaningless because the Board could always defer to the certificate of approval process.

SMC 25.12.590 is in the Control's and Incentives chapter of the SMC and states:

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Only the following factors may be considered in determining the reasonable return on a site, improvement or object:

A. The market value of the site, improvement or object in its existing condition taking into consideration the ability to maintain, operate or rehabilitate the site, improvement or object:

1. Before the imposition of controls or incentives, and

2. After the imposition of proposed specific controls and/or incentives;

B. The owner's yearly net return on the site, improvement or object, to the extent available, during the five (5) years prior to the imposition of specific controls and/or incentives;

C. Estimates of the owner's future net yearly return on the site, improvement or object with and without the imposition of proposed specific controls and/or incentives;

D. The net return and the rate of return necessary to attract capital for investment:

1. In such site, improvement or object and in the land on which the site, improvement or object is situated after the imposition of the proposed specific controls and/or incentives, if such information is available, or, if such information is not available,

2. In a comparable site, improvement or object and in the land on which such comparable site, improvement or object is situated; and

E. The net return and rate of return realized on comparable sites, improvements or objects not subject to controls imposed pursuant to this chapter.

SMC 25.12.750 is located in the chapter dealing with certificates of approval and states:

In considering any application for a certificate of approval the Board, and the Hearing Examiner upon any appeal, shall take into account the following factors:

A. The extent to which the proposed alteration or significant change would adversely affect the specific features or characteristics specified in the latest of: the Board approval of nomination, the Board report on approval of designation, the stipulated agreement on controls, the Hearing Examiner's decision on controls, or the designating ordinance;

B. The reasonableness or lack thereof of the proposed alteration or significant change in light of other alternatives available to achieve the objectives of the owner and the applicant;

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C. The extent to which the proposed alteration or significant change may be necessary to meet the requirements of any other law, statute, regulation, code or ordinance;

D. Where the Hearing Examiner has made a decision on controls and economic incentives, the extent to which the proposed alteration or significant change is necessary or appropriate to achieving for the owner or applicant a reasonable return on the site, improvement or object, taking into consideration the factors specified in Sections 25.12.570 through 25.12.600 and the economic consequences of denial; provided that, in considering the factors specified in Section 25.12.590 for purpose of this subsection, references to times before or after the imposition of controls shall be deemed to apply to times before or after the grant or denial of a certificate of approval; and

E. For Seattle School District property that is in use as a public school facility, educational specifications.

The hearing on this appeal involved one discrete determination: the determination as to whether the Board's recommended *controls* were proper. Despite defining how these hearings are to be decided, the Hearing Examiner inextricably relied upon the standards for *certificate of approval* hearings. The Hearing Examiner made a recommendation for controls that was not based upon the "control" hearing provisions, but rather based on the factors for "certificate of approval" hearings. Her decision should be overturned for making this error in law.

The Hearing Examiner's Findings and Recommendations also improperly change the structure of landmark preservation in Seattle and are inconsistent with the SMC. Every control recommended by the Board must, by the requirements of SMC 25.12.520, state circumstances that would require the Owner to obtain a certificate of approval before altering or changing the site/improvement if the controls are imposed. Yet the Hearing Examiner reasoned that because a certificate of approval can be sought to alter the building after the controls are imposed, controls in this situation cannot deprive the owner of reasonable economic return.

To accept this reasoning is to subvert the legislative process by rendering SMC

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25.12.570, 580 and 590 meaningless, as the *certificate of approval* process would essentially moot these *controls and incentives* provisions. In essence, upholding the decision is stating that these code sections are present for nothing more than window dressing.

Why, then, has the City Council so thoroughly legislated the concern about being deprived of reasonable economic use in the control section and done so in a different manner in the certificate of approval code? Not only has it drafted a number of ordinances relating to loss of reasonable economic return, it has provided that the ONLY appropriate time to appeal a control is immediately after the Board recommends a control. Waiting until after a certificate of approval process has been initiated would waive the Owner's ability to challenge the underlying control under most circumstances.[8]

C. The Hearing Examiner's Recommendations Prevent the Owner from Realizing a Reasonable Return on The Eitel Building in Violation of SMC 25.12.570, SMC 25.12.580 and SMC 25.12.590

The touchstone for deciding whether controls may be imposed on a designated landmark structure is the realization of a "reasonable return" on the property after imposition of the controls and available incentives, as provided by SMC 25.12.570. As the Board provided no contradicting evidence when it adopted its controls for the Eitel Building, if the below information, provided at the hearing and to the Board at the time of recommendation, is sufficient to show that there will be no reasonable return on this structure, the City Council should reverse the Hearing examiners decision and place no controls on the building that would prevent adding additional height to the building.

The only factors the Hearing Examiner may consider in determining the reasonable

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[8] Further, the Owner submitted the drawings from its Master Use Permit to the Board's Architectural Review Committee in 2007. (F.R. p.2, ¶10.) The ARC suggested that it would restrict any structure above the seventh floor. This shows that it is essentially futile to go through this process. The controls process is also supposed to be "collaborative" (see F.R. p.3, ¶11) but this "collaboration" has been nothing but a financial and psychological burden on the owner—constantly forced to provide more and more information and then receiving no response.

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return on a site are found in SMC 25.12.590. In the three years since it began negotiating with the Board on the Controls and Incentives Agreement, the Owner has provided substantial evidence concerning the impacts of controls that require preservation of the Eitel Building. *See generally* **Exhibit 1, Tabs 1 through 9**. These reports and cost estimates were updated to reflect changing market conditions and to supplement the evidence in response to questions raised by staff. Specifically, the Owner's appraiser, the O'Connor Consulting Group ("OCG") prepared its initial appraisal report and feasibility study in June, 2007. **Exhibit 1, Tab 2** (EITEL00191-00328). OCG then updated its analysis in May, 2008. **Exhibit 1, Tab 2** (EITEL00144-00190). OCG prepared supplemental analyses in May, September and October, 2009. **Exhibit 1, Tab 2** (EITEL00054-00143, 00009-00012, and 00001-00008). The Owner also engaged two cost estimators, Harvey Hendrickson from W.G. Clark Construction Company, and Sandra Matson, from Matson Carlson Associates. Given the current economic climate, the Owner's experts again updated their appraisal report and cost estimates for the April, 2010, hearing. *See* **Exhibit 1, Tabs 10-12** (EITEL00461-00725).

In spite of the evolving economic conditions, the conclusions drawn by the Owner's experts have been consistent and unchallenged by the Board with any substantive evidence. When applying each of the factors under SMC 25.12.590, the Owner's experts have repeatedly reached the same conclusion: imposition of preservation controls on the Eitel Building will leave the owner without a reasonable return. The following analysis reflects the evidence of the Owner's experts as provided at the hearing.

1. Market Value "Before" and "After" Imposition of Controls & Incentives: SMC 25.12.590(A)

Market value is a defined term under the Uniform Standards of Professional Appraisal Practice ("USPAP):

> The most probable price that a property should bring in a competitive and open market under all conditions requisite to a

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fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. **Implicit in this definition are the consummation of a sale as of a specified date** and the passing of title from seller to buyer under conditions whereby:

a) Buyer and seller are typically motivated;

b) Both parties are well informed or well advised, and acting in what they consider their own best interest;

c) A reasonable time is allowed for exposure in the open market;

d) Payment is made in terms of cash in U.S. dollars or in terms of financial arrangements comparable thereto; and

e) The price represents the normal consideration for the property sold, unaffected by special or creative financing or sale concessions granted by anyone associated with the sale."

Exhibit 1, Tab 11, p. 18 (EITEL00503) (emphasis added). Market value presumes the "highest and best use" of the property. *Id.*, **p. 19** (EITEL00504); *see* EITEL00554 for definition of the term; *see also* IN THE MATTER OF CONTROLS AND INCENTIVES FOR THE BON MARCHE STABLE BUILDING, LP-08-004, p. 7, ¶32.

a. Before Imposition of Controls & Incentives

The Owner's expert appraiser, Brian O'Connor, MAI, determined that the market value of the Eitel Building before imposition of the controls and incentives ranges from $2,500,000 (under its current vested rights)[9] to $1,650,000 (under current zoning)[10]. **Exhibit**

[9] In 2006, the Owner applied for a Master Use Permit ("MUP") (#3004150) for the development of a 22-story building with 92 residential units above 23,000 square feet of administrative office and 3,000 square fee of retail. Accordingly, the property currently enjoys vested rights for this development pursuant to SMC 23.76.010.E.2 and SMC 23.76.026. *See* **Exhibit 1, Tab 12** (EITEL00679). The Owner's MUP was placed on a two-year "Hold" in May, 2009 through a temporary program authorized by the City of Seattle and confirmed by the Department of Planning and Development on December 9, 2009. *See* **Exhibit 1, Tab 11** (EITEL00549).

[10] Under current zoning, the property would be entitled to support a 160-foot tall structure. While the property enjoys a vested right to build a 240-foot structure, Mr. O'Connor's feasibility analysis and market valuation *after* imposition of controls examined the 160-foot structure. *See* **Exhibit 1, Tab 11** (EITEL00583-00587).

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1, Tab 11 (EITEL 00490, 00582-00587). This valuation presumes that no controls would be imposed and reflects what a prospective buyer would be willing to pay for the property for redevelopment. *Id.* In reaching his conclusion, Mr. O'Connor relied on the sales comparison approach by examining nine and six properties comparable to the Eitel Building property for the vested rights and current zoning scenarios, respectively. **Exhibit 1, Tab 11** (EITEL 00490, 00558-00587). Mr. O'Connor's conclusions were accompanied by his certification that the appraisal was performed in accordance with USPAP and conformed with the standards and reporting requirements of the Code of Professional Ethics and Standards of Professional Practice of the Appraisal Institute. **Exhibit 1, Tab 11** (EITEL00588; EITEL00502-00507).

By contrast, the Board offered no evidence of market value before imposition of controls and incentives. The Board's witness, Peter Shorett, MAI, CRE, FRISC, acknowledged during testimony that he did not develop an opinion of "market value." In fact, he could not have determined market value, as defined by USPAP, given the indefinite date of "sometime in the future" and reliance on the creative financing arrangement involving Low-Income Housing Tax Credits ("LIHTC"). To date, the Board has never offered any evidence that contests Mr. O'Connor's conclusions on market value before imposition of controls.

b. After Imposition of Controls & Incentives

Mr. O'Connor concluded that the market value after imposition of controls and incentives is $0 (zero dollars), using the development approach to value. **Exhibit 1, Tab 12** (EITEL00706). In reaching his conclusion, Mr. O'Connor considered various use scenarios for the preservation of the Eitel Building, concluding that "under present and anticipated near-term market conditions, rehabilitation of the existing improvement for residential apartment and retail use would be considered to be the 'least infeasible' use."[11] **Exhibit 1,**

[11] Previous reports examined other rehabilitation scenarios, such as office, condominium and hotel use, which

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Tab 11 (EITEL00604). In support of his conclusion, Mr. O'Connor further stated:

> [T]he financial losses accrued in the rehabilitation project are greater than the underlying value of the property "before imposition of controls and incentives." Significantly, the estimated losses are substantially greater than the underlying value of the property, suggesting that a negative value might be supported under the assumption that the controls would represent a binding obligation of the owner to preserve the existing improvements. The analysis presented would indicate that such liabilities may, in total, reflect an absolute change in the magnitude of adjustment of $6,300,000 (the difference between +$1,650,000 and -$4,650,000) which would reduce the market value of the property to (a negative or minus) -$4,650,000.

Id. at EITEL00605. Thus, the actual financial impact to the Owner for rehabilitation of the Eitel Building would result in a negative value, requiring the owner to "pay a 'buyer' to take the property off his hands." *Id.*[12]

(1) Construction Costs

Mr. O'Connor's appraisal relied on the rehabilitation costs prepared by Sandra Matson of Matson Carlson Associates. **Exhibit 1, Tab 10** (EITEL00461-00487). For the apartment scenario, Ms. Matson concluded that the total construction costs would amount to $12,011,575. **Exhibit 1, Tab 10** (EITEL00461). The base construction costs amounted to $7,259,012. **Exhibit 1, Tab 10** (EITEL00464); *cf* **Exhibit 16** (comparing the totals less the contingency costs as equivalent as between the Board's witness, Steve Stroming, and the Owner's other cost estimator, Harvey Hendrickson). To the base cost, Ms. Matson added 15% as the "estimating/design contingency." *Id.* She also added 15% or $1,566,727 for the

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were submitted to the Board. *See* **Exhibit 1, Tab 2**, EITEL00029-00337). For each of these scenarios, Mr. O'Connor concluded that the economic return to the owner of the Eitel Building was less than zero. Indeed, the project costs for rehabilitation exceeded the market value at completion by over $3.3 million to $4.3 million dollars for the various scenarios. However, Mr. O'Connor concluded that current market conditions would render these other scenarios even more infeasible, and therefore limited his analysis to the apartment scenario.

[12] The Board noted during the hearing that the Owner submitted and continues to renew permits to develop the Eitel Building for office use. By contrast, Mr. O'Connor has concluded that, after imposition of controls, apartment use is the *least infeasible* use for the property. **Exhibit 1, Tab 12** (EITEL00710).

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owner's "Change Orders."[13]

The Board's witness, Mr. Stroming, questioned whether Ms. Matson's 15% "change order" addition was a valid assumption. As Mr. O'Connor testified, however, experts in the area of appraisals for historic preservation projects routinely add as much as 20% (or more), given the uncertainties and variables related to this type of construction. To avoid duplication of these added contingency entries, Mr. O'Connor lowered his "Developer's Contingency" to 5%, resulting in an overall change order contingency of 20%. *See* **Exhibit 1, Tab 12** (EITEL00697). Mr. O'Connor also made other adjustments to Ms. Matson's estimate, both downward and upward, resulting in a "direct cost estimate" to $12,011,915. *See* **Exhibit 1, Tab 12** (EITEL00695).

Mr. Stroming also presumed that "construction-ready" drawings existed for the redevelopment of the property. In support of his statement, he referred to the 2001 permit application drawings from the Owner on redevelopment of the Eitel Building as *office use*. **Exhibit 2.** However, no drawings exist and no permit has been obtained by the Owner for redevelopment as *apartment use*. Given this oversight by Mr. Stroming and his overreliance on inapplicable permit drawings, Mr. Stroming's estimate assumed construction contingencies that were too low.

(2) Incentives Available

Pursuant to the Board's Recommendation on Controls & Incentives, Mr. O'Connor relied on the following incentive programs:

- The Washington State "Special Tax Valuation for Historic Properties" program,
- The federal "20% Rehabilitation Tax Credit" program, and
- Sale revenues that may be derived from the City of Seattle's "Downtown Transferable Development (TDR) Program."

[13] Noteworthy is the fact that Mr. O'Connor's appraisal shows that the theoretical market value of the Eitel Building after imposition of controls is –$4,650,000. Even if Ms. Matson's "change order" contingency were *fully deducted* from the direct costs, the market value would still be over –$3 million.

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See **Exhibit 1, Tab 12** (EITEL00691); Board's Recommendations on Controls & Incentives, p. 2.[14] From each of these programs, Mr. O'Connor concluded that the total incentive value added is $2,565,000. The Board's expert, Mr. Shorett, similarly applied these three programs and also applied the LIHTC. A side-by-side comparison of the incentives is shown on Table 1 below.

Table 1 – Eitel Building Incentives

Incentive Program	Owner's Net Present Value	Board's Net Present Value
Sale Value of Federal 20% Rehabilitation Tax Credit	$2,220,000	$2,200,000
Washington State "Special Tax Valuation for Historic Properties"	$345,000	$90,000
Sale of Transferable Development Rights ("TDRs")	$0	$370,000
Sale Value of LIHTC	N/A	$8,870,000
Total Incentive Value Added	**$2,565.000**	**$11,530,000**

For the TDR program, Mr. O'Connor assigned no value for this incentive given the current market conditions. Mr. Shorett, by contrast, assumed the TDRs would be available at some point in the future, assuming rebounded market conditions, and attributed $370,000 as an incentive value from this program.

Aside from the sale value of LIHTCs as assumed by Mr. Shorett, the incentives values are comparable and the difference of $110,000 falls far short of the incentives needed to overcome Mr. O'Connor's estimated market value after imposition of controls of minus $4,650,000. *See* **Exhibit 1, Tab 12** (EITEL00706).

The Board's reliance on the LIHTC to bridge this considerable shortfall must be dismissed as not supported by substantial evidence. Moreover, Mr. Shorett's analysis does not yield a "market value" (either "before" or "after" imposition of controls) as required by

[14] The Board also identified in its recommendation incentives involving uses "not normally permitted in a particular zoning classification by means of an administrative conditional use" and "Building and Energy Code exceptions." No monetary value was attributed to either of these incentives by witnesses for either the Board or Owner. The Owner's witness, Robert Kovalenko, an architect, opined that the building and energy code exceptions would likely not result in any cost savings.

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SMC 25.12.590.A. Therefore, the Board's use of Mr. Shorett's conclusions is not supported by applicable law. Accordingly, the Board's recommended controls and incentives must be rejected as provided by SMC 25.12.560.B.

c. Summary of Market Value

Given the substantial construction costs, preservation of the Eitel Building is not economically feasible. As shown on Table 2 below, this results in a reduction of property value of 100% after imposition of controls compared to the "before" value of the Eitel Building, after applying all reasonable incentives. In actuality, however, the property owner would carry the debt equity for the construction costs that exceed the property's value after rehabilitation controls have been imposed.

Table 2 – Eitel Building Property Market Value
"Before" and "After" Imposition of Controls & Incentives

"Before" and "After" Market Values		
"Before" Controls & Incentives – Current Vested Rights (as of March 23, 2010)	$2,500,000	$447 / SF
"Before" Controls & Incentives – Current Zoning (as of March 23, 2010)	$1,650,000	$295 / SF
"After" Controls & Incentives (as of April 5, 2010)	$0	$0 / SF
Minimum Economic Impact to Owner	($1,650,000)	($295 / SF)

2. Yearly Net Returns for the Past Five Years Without Controls/Incentives: SMC 25.12.590(B)

The average net annual operating income for the Eitel Building was $94,365 over the past five years as shown on Table 3 below. *See* **Exhibit 1, Tab 12** (EITEL00708). For the past five years, the rise in operating expenses has outpaced that of income. *Id.* In fact, the trend of operating expenses has shown a considerable rise over reported expenses in prior years. *See e.g.,* **Exhibit 1, Tab 2** (EITEL00171, Pre-2005 operating expenses were less than $50,000 per year). In 2007, the owner of the Eitel Building suffered a net loss of nearly $20,000. *See* **Exhibit 1, Tab 12** (EITEL00708).

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Table 3—Owner's Yearly Net Returns for the Past Five Years

Eitel Building - Historical Income & Expense Analysis					
Year	**2005**	**2006**	**2007**	**2008**	**2009**
Gross Income	$196,655	$280,180	$210,821	$251,210	$213,630
Less: OPUS Payment	$0	-$80,000	$0	$0	$0
Gross Operating Income	**$196,655**	**$200,180**	**$210,821**	**$251,210**	**$213,630**
Operating Expenses					
Fixed Expenses					
Property Taxes	$17,689	$15,578	$22,696	$12,607	$10,648
Insurance	$2,592	$3,602	$6,060	$4,182	$3,067
subtotal	$20,280	$19,180	$28,757	$16,790	$13,715
Variable Expenses					
Repairs & Maintenance					
Supplies	$725	$3,642	$0	$5,632	$7,317
Equipment Rental	$0	$0	$0	$69	$0
Contract Labor	$3,131	$5,514	$49,032	$5,593	$9,329
Utilities	$7,729	$6,079	$7,674	$13,286	$8,185
Miscellaneous					
Parking	$0	$0	$0	$0	$0
Legal & Accounting	$450	$56,901	$145,079	$77,162	$67,420
Applicable Capital Expense	$0	$22,000	$0	$0	$0
subtotal	$12,034	$94,136	$201,786	$101,742	$92,251
Total Operating Expenses	**$32,315**	**$113,315**	**$230,542**	**$118,531**	**$105,966**
Net Operating Income	**$164,340**	**$86,865**	**-$19,722**	**$132,679**	**$107,664**
Average	$94,365				
Assessed Value	$951,600	$951,600	$1,717,800	$1,958,200	$2,237,800
Return against Assessed Value	17.3%	9.1%	-1.1%	6.8%	4.8%
Average	7.4%				

Exhibit 1, Tab 12 (EITEL00708).

Moreover, the building itself is fully depreciated, both functionally and structurally, and can therefore only offer continued diminishing returns to the property owner without significant property investment. *See* **Exhibit 1, Tab 12** (EITEL00707-00708). Net operating expenses are expected to increase significantly in the future, given the financial demands necessary to keep the building minimally serviceable.

The Board has offered no evidence to contest the Owner's net annual returns for the past five years.

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3. Estimated Future Net Yearly Returns With and Without Control/Incentives: SMC 25.12.590(C)

a. With Imposition of Controls & Incentives

With the imposition of controls and incentives, the Eitel Building would suffer a future net yearly return of -26.8% and an overall net return on equity of -82.0% for the apartment rehabilitation scenarios. **Exhibit 1, Tab 12** (EITEL00605).[15] The net **loss** for rehabilitation of the Eitel Building would be $6,609,200.

As Mr. O'Connor notes, the analysis of the Owner's future net return is based on the "least infeasible" of the possible uses to which the rehabilitated Eitel Building might be put. **Exhibit 1, Tab 12** (EITEL00710). The incentives available are simply insufficient to overcome the excessive cost of rehabilitation, which necessarily reduces the potential contributory value of the underlying land and building. As Mr. O'Connor noted:

> [T]he estimated losses are substantial enough that even the reduction of the assumed investment basis or cost of the property to an "after" value of $0 (zero) is insufficient to produce a profit or return on equity necessary to attract investment capital. Only when the assumed land basis ("after imposition of controls and incentives") is reduced to a negative value of -$4,650,000 would the project be expected to produce a rate of return that would be considered sufficient to attract investment capital.

Exhibit 1, Tab 12 (EITEL00710); *see* Table at EITEL00703 (illustrating a required land value to produce an overall net return on equity of +75% ~ the return necessary to attract investment capital).

To derive his conclusions, Mr. O'Connor specifically applied a feasibility approach

[15] Previous reports uncontested by the Board showed yearly returns of -18.1% and -17.1% for the two income-producing rehabilitation scenarios (apartment and retail/office). Because of the exceptionally high losses at the completion of construction, Mr. O'Connor estimated that it would take the Owner 25 years to 45 years after completion of the project to yield a profit with the expected income stream for these scenarios. Under the condominium scenario, the project loss would be over $4.3 million *after* the sale of all units. Moreover, the Owner would have required equity of nearly $6 million and $7.5 million to complete the preservation of the project under the office and apartment scenarios, respectively. *See* **Exhibit 1, Tab 2** (EITEL00010).

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to determine whether rehabilitation of the existing structure would generate sufficient revenue to produce a profit. His answer, supported in detail in his *Appraisal Consulting Report* (**Exhibit 1, Tab 12**) is unqualified: "The substantial losses indicated in the Feasibility Analysis are not believed to be either unrealistic or unusual given both the high costs associated with essentially 'rebuilding' the existing improvements and the loss of future development rights for the property." **Exhibit 1, Tab 12** (EITEL00710). Accordingly, rehabilitation of the Eitel Building in accordance with the Board's recommended controls and incentives is not feasible, leaving the Owner with a negative return and depriving him of economic use of the property.

The Board offered evidence through Mr. Shorett's *Limited Use Appraisal Consulting Report* of gross and net returns on equity exceeding 100%. **Exhibit 10**, Attachment. However, Mr. Shorett's conclusions are based on speculation, inaccuracies and supporting analysis that does not conform to applicable appraisal standards under USPAP. To create his rates of return, Mr. Shorett uses an implied residual land value, which as both Messrs. O'Connor and Gibbons testified, is distinct from a "market value" required under the Code. The validity, reliability and relevancy of Mr. Shorett's conclusions are therefore questionable.

b. Without Imposition of Controls & Incentives

As noted previously, without imposition of controls, the highest and best use of the property would be to "hold for future development," because current market demand does not support feasible redevelopment. Given this limitation, Mr. O'Connor determined that the future net yearly return without controls and incentives would be 20.1%. **Exhibit 1, Tab 12** (EITEL00709).[16] The basis for his determination was a sale of the property to a hypothetical

[16] Under previous reports submitted to the Board, the net annual return for the apartment use scenario was estimated at 3.3%, with an equity cash flow of $306,723. The gross profits at the completion were expected to amount to $3,875,000 and $5,720,000 for the apartment and condominium uses, respectively. The overall rates of return would therefore range from 111.9% to 165.1%. **Exhibit 1, Tab 2** (EITEL00173-00174).

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buyer at the market value of $1,650,000. *Id.*

The Board offered no evidence supporting the net future returns without imposition of controls and incentives.

4. Net Return and Rate of Return Necessary to Attract Investment Capital and Comparable Sites: SMC 25.12.590(D) and (E)

a. With Imposition of Controls & Incentives

The required rates of return necessary to attract investment capital for projects with imposition of controls and incentives are slightly higher than for those projects without. This is because the development risks associated with preservation of an historic landmark would be construed by most investors in the marketplace as having a slightly higher investment risk.

There are several reasons why the market would require a greater return for historically designated properties:

- Historically designated properties have higher than typical maintenance costs in the long run;
- Historically designated properties lack a future reversion value based on the future development potential of the underlying land; and
- The costs associated with rehabilitation of a 100-year old building are very difficult to estimate and cost overruns are not unusual.

Exhibit 1, Tab 12 (EITEL00711).

Mr. O'Connor determined that a 125% gross return on equity and a 10% to 20% return on cost after imposition of controls and incentives would sufficient to attract investment capital. **Exhibit 1, Tab 12** (EITEL00711); *see also In the Matter of Controls and Incentives for the Bon Marche Stables*, Findings and Recommendations of the Hearing Examiner for the City of Seattle, LP-08-004, p. 10. As shown above, the magnitude of the expected losses was sizable enough that even a 100% reduction of the market value of the property would not be likely to produce sufficient returns. *See* **Exhibit 1, Tab 12**

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(EITEL00703). As noted in the preceding section, the return on equity for preservation of the Eitel Building is -82%, with a net annual return of -26.8%. **Exhibit 1, Tab 12** (EITEL00605). Given the negative returns on equity and annual rates of return, preservation of the Eitel Building could not be expected to attract investment capital.

The Board offered no evidence regarding the rate of return necessary to attract investment capital with imposition of controls.

b. Without Imposition of Controls & Incentives

Despite the current economic climate, market conditions continue to favor similar rates of return as in the recent past. The return requirements in the market reflect a variety of factors that include the scale and perceived risk of the investment venture. In general, however, Mr. O'Connor concludes that new real estate development ventures in downtown Seattle core neighborhoods tend to require an overall (or gross profit generated) net annual return on equity of between 20% and 25%. **Exhibit 1, Tab 12** (EITEL00711). As noted above, Mr. O'Connor estimated yearly return on equity of 20.1% for the hypothetical sale of the property.

The Board offered no evidence regarding the rate of return necessary to attract investment capital without imposition of controls.

IX. CONCLUSION

The City Council is empowered to reject or modify the controls recommended by the Board. Due to the mishandling of this process by the Hearing Examiner, the expense spent by the Owner as the Board refused to develop any support for its desire to implement the "standard" controls, and the clear evidence showing the financial ruin that will be caused if the controls are not rejected, the Owner requests that City Council reject the controls completely.

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Dated this 8th day of November, 2010.

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By: _____
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CERTIFICATE OF SERVICE

I hereby certify that on the 8th day of November, 2010, I caused to be served the foregoing *1507 Group's Appeal of Hearing Examiner's Recommendation* on the following parties at the following addresses:

City Clerk
Attention: Sally J. Clark
c/o Ketil Freeman
Seattle City Council
600 Fourth Avenue, Floor 3
Seattle, WA 98124

Roger D. Wynne
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Seattle City Attorney's Office
600 Fourth Avenue, 4th Floor
Seattle, WA 98104

by:

- ☐ U.S. Postal Service, ordinary first class mail
- ☐ U.S. Postal Service, certified or registered mail, return receipt requested
- ☒ hand delivery
- ☐ facsimile
- ☐ electronic service
- ☐ other (specify) _____

James C. Anderson
Secretary to Lawrence A. Costich

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BEFORE THE SEATTLE CITY COUNCIL

In the Matter of the Appeal of : THE 1507 GROUP, LLC, APPELLANT	Hearing Examiner File: LP-10-001 DEPARTMENT OF NEIGHBORHOODS' RESPONSE BRIEF

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I. INTRODUCTION AND SUMMARY

Respondent Department of Neighborhoods ("Department") respectfully asks the Council to affirm the controls and incentives ("C&I") recommended by the Hearing Examiner for the Eitel Building and to enact an ordinance containing the C&I. The owner of the Eitel Building, 1507 Group LLC ("Owner"), has not carried its burden of proving that the Council should reject or modify the recommended C&I.

The recommended C&I would direct the Owner not alter the exterior of the Building without first obtaining a certificate of approval ("CoA") from the Landmarks Preservation Board ("Board"). At this point, one cannot know what alterations the Board would approve through the CoA process. But two facts are clear: (1) the Owner and his experts admit that the Owner can realize a reasonable economic return and use if the owner can sell the air rights above the Building or build above the existing shell while preserving the two key facades; and (2) those outcomes are not precluded by the language of the recommended C&I, the nature of the CoA process generally, or the partial CoA process conducted for the Eitel Building. Nevertheless, the Owner argued that the C&I would necessarily leave the Owner with no reasonable economic return or use. To support that argument, the Owner presented expert analysis and testimony that was expressly premised on the assumption that the C&I would limit future alterations to the shell of the existing Building. The Examiner correctly concluded that the Owner cannot sustain its burden through evidence that is based on a false premise. The Council should affirm that straightforward conclusion.

Because of that conclusion, the Examiner also correctly concluded that she did not need to sort through the voluminous expert debate over the Owner's contention the C&I will leave the Owner with no reasonable economic return and use. That debate is moot because it was

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constructed on the false premise that the C&I would limit future alterations to the shell of the existing Building. The Council should therefore follow the Examiner's lead by avoiding that debate as well.

Hobbled by a case premised on a fatally false assumption, the Owner's opening brief goes after the Examiner. That tactic is fruitless because the Examiner followed the clear language of the Code.

Because the Owner cannot sustain its burden of proof, the Department respectfully asks the Council to affirm the Examiner's recommendation and enact an ordinance containing the C&I.

II. FACTS

This appeal is based on the record compiled by the Examiner. SMC 25.12.630.C. The Examiner's Findings and Recommendation recite the relevant facts with citations to the record. Rather than repeat those factual findings here, the Department is attaching a copy of the Examiner's decision as **Appendix A**. The Department respectfully asks the Council to review that decision.

III. ARGUMENT

The Owner bears the burden of proving that the Council should reject or modify the Examiner's recommended C&I. SMC 25.12.630.C. The Owner cannot sustain that burden because the Owner's argument is based on a false assumption and because the Owner's criticisms of the Examiner lack merit.

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A. The Owner cannot meet its burden on the false assumption that the recommended C&I would necessarily force the Owner to keep all future development within the shell of the existing Building.

The challenge faced by the Owner in this case is to demonstrate that the imposition of the recommended C&I would necessarily prevent the Owner from realizing a reasonable return or deprive the Owner of a reasonable economic use. SMC 25.12.570, .580. The Owner cannot do that because the recommended C&I would do nothing more than require the Owner to obtain a CoA before making exterior alterations. There is nothing on the face of the recommended C&I, in the nature of the CoA process generally, or in the specific CoA process conducted in part for the Eitel Building that suggests that, after imposition of these C&I, the only alterations that would be allowed would be ones that keep the Building within its existing shell. Nevertheless, the Owner's entire case rests on the premise that the recommended C&I would limit future development to the existing shell. Because that premise is false, the Owner cannot demonstrate that imposition of the recommended C&I would necessarily deny the Owner a reasonable return or use. The Council should enact the C&I and then let the CoA process proceed as intended, after which a genuine assessment can be made of the Owner's economic return and use.

1. As a general matter, the CoA process involves a cooperative balancing of goals and has resulted in projects where a new structure is built behind a designated façade.

The CoA process is set forth in SMC 25.12.670 - .750. The elements relevant to a CoA decision are not absolute; they involve a weighing of factors:

> A. The extent to which the proposed alteration or significant change would adversely affect the [specified] features or characteristics...;
>
> B. The reasonableness or lack thereof of the proposed alteration or significant change in light of other alternatives available to achieve the objectives of the owner and the applicant;

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> C. The extent to which the proposed alteration or significant change may be necessary to meet the requirements of any other law, statute, regulation, code or ordinance; [and]
>
> D. Where the Hearing Examiner has made a decision on controls and economic incentives, the extent to which the proposed alteration or significant change is necessary or appropriate to achieving for the owner or applicant a reasonable return on the site, improvement or object, taking into consideration the factors specified in Sections 25.12.570 through 25.12.600....

SMC 25.12.750. The language of the Code, in short, does not dictate certain outcomes of the CoA process. It does not require preservation of all designated features at all costs.

The testimony of Department staff person Sarah Sodt provided an insight into the Board's practice of applying this Code language. The process starts with the Architectural Review Committee ("ARC"):

> The ARC is a subcommittee of the Board composed of members with architectural expertise. The ARC is available to meet with an owner to review a proposal, and provide feedback and suggestions on it, before the owner seeks a Certificate of approval from the full Board. The process is collaborative, and the goal is to achieve a design solution that meets both the owner's needs and the Board's goal of preserving the designated historic features. Testimony of Sarah Sodt, 4/15/10 at 1:22.

Findings and Recommendation ("F&R"), Finding 11. Because of this collaboration, the CoA process may result in the destruction of some portion of a designated exterior of a landmark. Ms. Sodt provided examples of recent Board decisions on CoA applications that involved the preservation of one or more façades, while allowing a different and/or taller structure to be built behind:

> [Ms. Sodt] testified that the Board has granted certificates of approval that resulted in the destruction of some designated features of landmark buildings when the aspects of the buildings that remained were sufficient to convey their historical importance. [She] cited two recent examples: the Pacific McKay Ford Building on Westlake Avenue, where the primary facades were removed and are in storage for future installation on a new development; and the Terminal Sales Annex Building at 1931 Second Avenue, a narrow building for which the Board approved retention of the street-facing facade and the addition of a multi-story

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tower atop the landmark. Testimony of Sarah Sodt, 4/15/10 at 1:22-1:26 and 2:20. She did not know of any certificate of approval application for construction of additional stories atop a landmark that has been denied. Testimony of Sarah Sodt, 4/15/10 at 2:22.

F&R, Finding 13.

2. The CoA and C&I processes here left open the possibility that, after imposition of the recommended C&I, the Owner could build a taller structure behind the preserved south and east façades.

The Owner's actual experience with the CoA process for the Eitel Building is consistent with the Board's general approach described by Ms. Sodt. The Owner initiated the CoA process, albeit half-heartedly. "Working with an architect not known to have experience with historical structures," the Owner presented to the ARC a proposal for a 22-story tower built immediately behind the preserved south and east façades of the Eitel Building. F&R, Findings 9-10, 15. The ARC did not order the Owner to return only with designs that remained within the existing shell of the Building. Id., Finding 15. To the contrary, and consistent with the Code calling for an exploration of "other alternatives available to achieve the objectives of the owner," the ARC asked the Owner to return with alternatives based on the tower-behind-preserved-façade concepts that would involve fewer stories and explore the possibility of setting the tower back. Id. "The Owner chose not to return to the ARC with a revised design proposal" and withdrew from the cooperative ARC process after the initial ARC consultation. Id., Finding 18. The Owner ultimately withdrew the CoA application altogether, even though the Owner still has a Master Use Permit ("MUP") application pending with the Department of Planning and Development. Id., Findings 24-25.

But even as the C&I process worked through the Board without a companion CoA application, the Board preserved the possibility of the tower concept. The staff report to the Board noted that the west façade was "secondary" and that the C&I should therefore expressly

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state that infill of the light well on that façade was not precluded. Ms. Sodt testified that staff would also likely advise the Board that the north façade—which now abuts a tower located on the property to the north—is "secondary' and not necessary to meaningfully preserve the designated features of the Eitel Building. See generally, id., Finding 3; Exs. 26 and 32.

None of this is to say that the Board must or would approve a 22-story tower behind the preserved east and south façades of the Eitel Building. Likewise, none of this is to say that a 22-story tower would pass muster under other City review, including SEPA and design review. However, nothing yet precludes a tower on this property. See F&R, Concl. 8.

3. The Owner assumed incorrectly that imposition of the recommended C&I would limit future alterations to ones within the shell of the existing Building.

The history of the Board's involvement with the Eitel Building proves that there is no basis in law or fact for assuming that imposition of the recommended C&I in this case would necessarily limit the Owner to remaining within the existing shell of the Eitel Building.

Nevertheless, the Owner bases its case on exactly that assumption. The 2010 report of the Owner's appraiser, Mr. O'Connor, notes that, because no copy of the proposed C&I had been presented for his review, he had to proceed with "the assumed obligation [after imposition of C&I] to preserve the exterior perimeter of the existing improvements...." Ex. 1, Tab 12 at 626.[1] He included this as an "extraordinary assumption" in his report, and added that "[s]hould it be discovered that the anticipated controls differ from those assumed; the appraiser reserves the right to modify the conclusions set forth in this report." Id. Mr. O'Connor included similar assumptions and caveats throughout his work on this matter. F&R, Findings 16-17, 20, 30. The

[1] Page reference to Exhibit 1 documents are to the "EITEL" Bates numbers.

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Owner's principal, Mr. Nimmer, shared Mr. O'Connor's assumption that imposition of the C&I would limit him to, at most, perhaps a penthouse addition to the Building. Id., Finding 22.

4. There is no dispute that, without a requirement to limit future alterations to inside the existing shell, the Owner could possibly realize a reasonable return and maintain a reasonable economic use.

Given the Owner's misplaced reliance on this ultimately false assumption, the Owner was forthright in demonstrating two ways that it could realize a reasonable return and maintain a reasonable economic use were it not for the presumed requirement to limit development to within the existing shell.

First, the Owner believes he could build a tower behind the existing south and east façades.[2] Mr. O'Connor's 2008 report analyzed the 22-story project that the Owner presented to the ARC and memorialized in the still-pending MUP application, see Ex. 29, and determined that the project would be profitable for a developer even after paying the Owner nearly $3.5M for the land. Ex. 2 to Ex. 1 at 149, 174-175. Although Mr. O'Connor did not rerun that analysis in 2010, he concluded that the highest and best use would be to hold the property for future apartment development, either under the 22-story tower-behind-the-façades scenario in the MUP application (currently worth $2.5M to the owner) or under a 16-story scenario (currently worth $1.65M). Ex. 1, Tab 11 at 493, 555.

Second, the Owner and its appraiser conceded that if historic controls did not deprive the Owner of air rights, the potential sale of those rights to the owner of the abutting condominium

[2] Even though this is the Owner's position, the Examiner concluded "we do not know with certainty whether a tower can be built atop the landmark, and there is no evidence in the record on whether development available to the Owner through the MUP and certificate of approval processes would provide the Owner with a reasonable return and a reasonable economic use." F&R Concl. 10. But whether a tower actually could be built, the fact remains that the Owner believes one can be built at a profit and has maintained a permit application with DPD for a tower. Those contentions and that application are fatal to the Owner's claim that the proposed C&I, which do not preclude a tower, necessarily leaves the Owner with no reasonable economic return or use.

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development would make it profitable to undertake renovation within the existing shell of the Eitel Building:

> [T]he Owner acknowledged that if controls on the building did not prevent an increase in building height, the air rights above the building would be valuable to the owners of adjacent buildings. As an alternative to a tower atop the existing building, the Owner agreed that the air rights could be sold to help fund renovation of the existing building. Testimony of Richard Nimmer, 4/13/10 at 11:18. The Owner's appraiser agreed that a purchase of air rights could make building renovation possible. Testimony of Brian O'Connor, 4/14/10 at 11:54.

F&R, Finding 22.

Nothing in the recommended C&I precludes either building higher behind two façades, or selling the air rights and keeping the Building at its existing height, both of which the Owner contends could lead to a profitable redevelopment. Because of that, the Owner is unable to sustain its burden of proving that the mere imposition of the recommended C&I would necessarily prevent the Owner from realizing a reasonable return or deprive the Owner of a reasonable economic use.

The CoA process should be given an opportunity to play out the way the Council intended it, and the Board customarily conducts it. Part of that process involves applying the same limitations that the Owner raises now: that the Owner should not be prevented from realizing a reasonable return or deprived of a reasonable economic use. See SMC 25.12.570.D. Definitively assessing those limitations should occur after consideration of alternatives by the Owner and the Board through the give-and-take of the CoA process. The limitations cannot be assessed now, under the false all-or-nothing premise currently assumed by the Owner.

In light of that, the Examiner correctly concluded: "Because all of the Owner's evidence is based on an invalid assumption, the Owner has not met the burden of proving that the Board's

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recommended controls and incentives should be rejected or modified." F&R, Concl. 12. The Council should reach the same conclusion and vote to enact the recommended C&I.

5. The Owner's various attempts to evade this conclusion are unpersuasive.

The Owner does not challenge the Examiner's factual findings quoted and cited above. Instead, the Owner makes five attempts to sidestep the conclusion that necessarily flows from those facts: that the imposition of C&I, standing alone, does not deprive the Owner of a reasonable economic return or use. None of those attempted evasions succeeds.

First, the Owner resorts to an unsupported falsehood. In a footnote intended to suggest the futility of any CoA process, the Owner states: "The ARC suggested that it would restrict any structure above the seventh floor." Opening Brief at 21 n.8. The Owner cites no record evidence for this statement. It is contradicted by the Examiner's finding, supported by citation to Ms. Sodt's testimony: "The ARC suggested that the architect consider an alternative that reduced the tower height and explore a tower setback. The ARC did **not** state that the design needed to stay within the existing shell of the building. Testimony of Sarah Sodt, 4/15/10 at 1:28-130." F&R at Finding 15 (emphasis added).

Second, the Owner slides into another footnote the assertion that its principal, Mr. Nimmer, testified that setting the tower back from the perimeter would "effectively render an addition as infeasible." Opening Brief at 6 n.3. The Examiner made no such finding and the Owner provides no citation to the recording of Mr. Nimmer's substantial testimony to allow anyone to assess the Owner's characterization of that testimony. Furthermore, Mr. Nimmer is not an expert, so could not have established as a fact the infeasibility of any particular tower design. Most crucially, the Owner's appraisal expert was clear that a shorter tower (16 stories instead of the 22 proposed to the ARC) would be feasible and profitable. F&R, Concl. 29. A

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shorter tower would also have been responsive to the ARC's suggestion to explore a reduced-height tower.

Third, the Owner misconstrues the Examiner's point. The Owner criticizes the Examiner for supposedly confusing the process for obtaining a CoA with the process for determining C&I. As proof, the Owner shows that the Examiner quoted and discussed SMC 25.12.750 (also quoted above), which lists the factors the Board is to weigh when making a CoA decision. See Opening Brief at 8, 18-21. The Examiner's purpose in citing the CoA factors was clear, and clearly not what the Owner makes it out to be. Just like the argument above, the Examiner discussed those factors to demonstrate that nothing in the CoA process would preclude the Owner from building outside the existing shell of the Building. That was the logical predicate to concluding that the recommended C&I—which do nothing more than direct the Owner to go through the CoA process before altering the exterior of the Building—do not necessarily deprive the Owner of a reasonable economic return or use.

Fourth, the Owner's efforts to blame the Board are thwarted by the record. The Owner complains that the process of negotiating C&I was "nothing but a financial and psychological burden on the owner" who had to engage in "a vain attempt to meet the Staff's ever changing and vague comments on the documents and feasibility studies commissioned by the Owner," all to be met by a decision by the Board "without providing any real explanation." Opening Brief at 6, 9, and 21 n.8. In addition to being unsupported by citations to the record, these contentions paint a picture that the record belies. For the Owner, the only good control is no control. In the Owner's own words, it had but one mission in the C&I negotiation process: to "challenge the imposition of **any** controls, since rehabilitating the building is prohibitively expensive." Opening Brief at 6-7 (emphasis added). The evidence at the hearing about the Owner's mission

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was so clear that the Examiner concluded: "During the intervening two years [after the Owner withdrew its CoA application], the Owner has directed resources toward convincing the Board that **any** controls and incentives placed on the landmark would prevent the Owner from realizing a reasonable return and deprive the Owner of a reasonable economic use." F&R, Concl. 10 (emphasis added).[3] The Owner should not blame the Board or its staff for being both overwhelmed and unconvinced by the series of dense appraiser and other expert reports and technical documents produced by the Owner in its effort to block any controls. Those materials covered roughly 450 pages by the time the matter reached the Board. See Ex. 2 to Ex. 1 (letter of Dec. 15, 2009, detailing the EITEL-numbered documents). Contrary to the Owner's suggestion, individual Board members did explain why they rejected the Owner's attempt to block any control, as a review of the 19 pages of minutes of the Board's meeting demonstrates. See Ex. 33.

Finally, the Owner requests a pass on the CoA process altogether. In yet another footnote, the Owner suggests:

> To the extent the City Council interprets that the element to be preserved under the Eitel Building's landmark designation is its façade and that the controls imposed do not require a certificate of approval for any additions above the existing building height, the City Council can modify the Hearing Examiner's recommendation on controls and incentives accordingly. Thus, the Owner would be free to additional [sic.] development above the structure and no certificate of approval would be needed to do so.

Opening Brief at 8 n.4. This would defeat the purpose of the CoA process. Context matters for historic preservation. The factors the Board applies are designed to discern additions that are

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[3] The drumbeat in the Owner's correspondence and reports to the Board was a consistent message that no controls would work. See, e.g., Ex. 2 to Ex. 1 (Dec. 15, 2009: "As we expressed to you..., we believe the preservation of the Eitel Building cannot be accomplished in a manner that would leave the owner with a reasonable economic use of the building.... To the extent the...Board fails to reach the same conclusion, we will be forced to declare an impasse."); Ex. 1 at 1 (Nov. 12, 2009); Ex. 1 at 58 (May 8, 2009).

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sympathetic to designated features from those that are inappropriate. See SMC 25.12.750 (quoted above). Because the Owner abandoned the CoA process, there is currently no basis for predicting what type of addition the Owner would construct. This again only underscores the conclusion that the Council should enact the recommended C&I so that the CoA process can proceed as the Council intended it to.

B. Because the Owner's expert testimony was based on a false assumption, the Council need not consider the record regarding the Owner's contention about the loss of a reasonable economic return and use.

The bulk of the Examiner hearing—including multiple rounds of expert testimony—was dedicated to the Owner's contention that the recommended C&I would deprive the Owner of a reasonable economic return and use. But as the Examiner correctly concluded, that debate was academic because "[t]he Owner's entire case, including all the work of the Owner's appraiser, rests on the premise that the Board's recommended controls would limit any development of the property to the shell of the existing building. Yet there is no evidence in the record to support that premise." F&R, Concl. 6. "Because all of the Owner's evidence is based on an invalid assumption, the Owner has not met the burden of proving that the Board's recommended controls and incentives should be rejected or modified." F&R, Concl. 12.

The Council should reach the same conclusion and, like the Examiner, refrain from delving into the remainder of the voluminous, technical record that ultimately proved to be based on a false premise.

But even if the Council wanted to explore that record without the benefit of having been able to assess witness credibility directly, and even if the Council wanted to indulge the false assumption that C&I would limit the Owner to the existing shell of the Building, the Council would have to conclude that the Owner failed to sustain its burden of proving that it would be

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left with no reasonable economic return or use. Because the Council need not dig through the record, the Department will not clog this brief with the details that undermine the Owner's arguments about no reasonable economic return or use. Rather, in case the Council would like to see those details, **Appendix B** to this brief contains the Department's alternative argument made to the Examiner—an argument on which the Examiner never needed to rule.

A few aspects of the Owner's opening brief on this issue merit response here. First, the Council should look skeptically on one-sided citations in the opening brief to the Owner's experts' reports. Each expert document in the record was subject to cross-examination. The Council should not treat the characterization of a document as unvarnished truth without first considering the testimony about that document.

Second, the Council should be wary of characterizations of the testimony without citation to the recording or transcript of that testimony. Because the Examiner observed all of the testimony and was able to assess the accuracy of counsel's characterization of it, detailed citations to the recording were not necessary in the briefing below. The Council does not have that ability.

Third, no one can review the record and agree with the Owner that "the conclusions drawn by the Owner's experts have been...unchallenged by the Board with any substantive evidence." Opening Brief at 22. As summarized in Appendix B, the Department's experts offered substantive evidence that directly challenged many of the key conclusions reached by the Owner's experts.

Finally, the Owner cannot dismiss as mere "speculation" the testimony of the Department's expert whose professional opinion was that low-income housing tax credits should be considered in the valuation of this property. All experts used their professional judgment,

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which cannot be confused with speculation. More importantly, the Owner's counsel could have raised an objection to the expert's testimony on the grounds of speculation—counsel either did not do so, or was overruled and has not cited that as an error on appeal. If it was speculation, the time to resolve that matter was before the Examiner, not now. As a matter of law, the testimony was not speculative.

C. The Examiner followed the letter of the Code by ruling that the Owner faces a significant burden of proof based on the record before the Examiner.

Necessarily boxed in by the fact that the Owner's case was premised on a fatally false assumption, the Owner goes after the Examiner by assailing the standard of review and burden of proof she employed. These arguments are unpersuasive because the Examiner followed the clear language of the Code.

1. The Examiner applied the Code correctly.

The Examiner correctly applied the language of the Code section that establishes the procedure, standard of review, and burden that she must use when entertaining an appeal of recommended controls:

> A. Proceedings before the Hearing Examiner shall be in accordance with the procedures for hearings in contested cases pursuant to the Administrative Code, Chapter 3.02 of the Seattle Municipal Code, and the Hearing Examiner's Rules of Practice and Procedure in effect at the time of the proceeding, except as such procedures are modified by this chapter.
>
> B. The Board's recommendation on proposed controls and incentives must be supported by applicable law and substantial evidence in the record. The appellant bears the burden of proving that the Board's recommendation should be rejected or modified.

SMC 25.12.560. This Code section establishes three key elements, all of which the Examiner employed.

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First, Subsection A sets the procedures. Through its reference to the Administrative Code, Subsection A brings to bear SMC 3.02.090, which establishes the procedures the Examiner must follow in contested "hearings," including the creation of a formal "record" and adherence to other elements that resemble a judicial trial. It makes clear that the Examiner is to base her findings of fact "exclusively" on the record created through her hearing:

> A. In any contested case all parties shall be afforded an opportunity for **hearing**....
>
> B. Notice of such **hearing** shall include...:
>
> D. Opportunity shall be afforded all parties to respond and present evidence and argument on all issues involved....
>
> F. The **record** in a contested cause shall include:
>
> 1. All pleadings, motions, and intermediate rulings;
>
> 2. Evidence received or considered;
>
> 3. A statement of matters officially noticed;
>
> 4. Questions and offers of proof, objections, and ruling thereon;
>
> 5. Proposed findings and conclusions;
>
> 6. Any decision, opinion, or report by the examiner presiding at the **hearing**.
>
> G. Oral proceedings shall be electronically recorded. A copy of the **record** or any part thereof shall be transcribed and furnished to any party to the **hearing** upon request therefor and payment of the reasonable costs thereof.
>
> H. **Findings of fact shall be based <u>exclusively</u> on the evidence and on matters officially noticed**....
>
> J. The examiner presiding at the **hearing** shall admit and give probative effect to evidence which possesses probative value commonly accepted by reasonably prudent men in the conduct of their affairs, and shall give effect to the rules of privilege recognized by law.
>
> K. All evidence, including records and documents in the possession of the agency which the examiner desires to consider, shall be offered and made a part

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of the **record** in the case, and no other factual information or evidence shall be considered in the determination of the case.

L. Examiners may take notice of judicially cognizable facts and of general, technical, or scientific facts within their specialized knowledge in the evaluation of the evidence presented to them; provided, that parties shall be notified during the **hearing**, or by reference in preliminary reports or otherwise, of the material so noticed, and they shall be afforded an opportunity to contest the facts so noticed.

M. Every party shall have the right of cross-examination of witnesses who testify, and shall have the right to submit rebuttal evidence.

SMC 3.02.090 (emphasis added). To reinforce the requirement that the Examiner must base all of her decisions "exclusively" on the record established in her hearing, the Code specifically orders the Examiner to base her decision regarding C&I "[o]n the basis of all the evidence presented at a hearing...." SMC 25.12.570.

Second, Subsection B of SMC 25.12.560 sets a two-part standard of review. The legal part of the standard asks whether the Board's recommendation is "supported by applicable law."[4] The factual part of the standard asks whether the Board's recommendation is supported by "substantial evidence in the record," which is established through the Examiner's trial-like process.[5]

Finally, Subsection B also places the burden of proof squarely on the shoulders of the appellant challenging the Board's recommendation: "The appellant bears the burden of proving that the Board's recommendation should be rejected or modified." Id. In other words, unless the

[4] Under an "applicable law" standard, the Examiner retains the ultimate authority to interpret legal issues *de novo*. See Mall, Inc. v. City of Seattle, 108 Wn.2d 369, 377-78, 739 P.2d 668 (1987) ("It is a well established rule of statutory construction that considerable judicial deference should be given to the construction of an ordinance by those officials charged with its enforcement.");

[5] "Substantial evidence" is a deferential test that entails a relatively low threshold of proof. See Sunderland Family Treatment Servs. v. City of Pasco, 127 Wn.2d 782, 801, 903 P.2d 986 (1995). Substantial evidence is merely "a sufficient quantity of evidence to persuade a fair-minded person of the truth or correctness of the order." City of Redmond v. Central Puget Sound Growth Mgmt. Hearings Bd., 136 Wn.2d 38, 46, 959 P.2d 1091 (1998).

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appellant does a sufficient job of marshalling the law and facts under the standard of review, the Examiner must affirm the Board's recommendation.

The Examiner adhered to all three of the Code's clear procedural mandates. First, she conducted the trial-like "hearing" at which she created the "record." Second, she applied the "applicable law and substantial evidence" standard, hewing "exclusively" to the record created at her hearing. Finally, she held the Owner to its burden of proof.

2. The Owner's various attacks on the Examiner are meritless.

The Owner's criticisms of the Examiner lack merit. They are premised on a misunderstanding of the language and structure of the Code.

a. The relevant record is the one established by the Examiner.

The Owner argues that, because SMC 25.12.560.B dictates that the Board's recommendation must be supported by "substantial evidence **in the record**," the Code orders the Examiner to apply some record established by the Board. The Owner fails to appreciate that only the Examiner may establish the record relevant to the Examiner's decision on the Board's recommendation. In SMC Chapter 25.12, one finds the words "hearing" and "the record" in provisions dealing with the Examiner's procedures. See, e.g., SMC 25.12.540, .560, .610. Most crucially, the immediately preceding subsection (SMC 25.12.560.A, quoted above) orders the Examiner to follow SMC 3.02.090 (also quoted above), which directs the Examiner to employ trial-like procedures to establish "the record" and to base her factual findings "exclusively" on that record. The reference in Subsection B to "the record" must be read consistently with the same "record" demanded by Subsection A. The Owner's interpretation is also at odds with SMC 25.12.610, which orders the Examiner to file her recommendation on controls within 15

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days of the close of "the record." If "the record" refers to some record established by the Board, there would be no way for the Examiner to comply with this order.

It makes sense that Code directs the Examiner to base her decision exclusively on the record created at her hearing. Consisting of eleven volunteers, none of whom must be an attorney, the Board is ill-designed to conduct a trial or maintain a rigorous record. See SMC 25.12.270. That is why the Code directs the Board to conduct its business through "meetings," not "hearings." See, e.g., SMC 25.12.330 (in general), .500 (meeting on agreed controls and incentives), and .720 (meeting on certificates of approval).[6] Specific to this case, the Board holds a "meeting" on a staff recommendation for controls if negotiations fail to reach an agreement with the owner. SMC 25.12.490. After that meeting, if someone objects to the Board's recommendation, that person is entitled to the due process safeguards built into the Examiner's hearing process, which results in a comprehensive, well-organized record for subsequent appeal. That is what the Code sensibly requires and what the Examiner provided.

b. The Examiner must take a *de novo* approach to the factual record.

The Owner misses the Examiner's point when criticizing her for allegedly applying a *de novo* standard of review. The Examiner, in fact, applied the "supported by applicable law and substantial evidence" standard required by the Code. See, e.g., F&R, Concl. 3-4. She invoked the phrase "*de novo*" to describe only the nature of the factual "record" she must apply to the "substantial evidence" standard, and only as a way to summarize the points just made above: her

[6] "Hearing" and "record" appear in the heading of SMC 25.12.340, which deals with Board meetings. However, the text of that section speaks only of Board "meetings," not "hearings." "Meeting" should control because the Council specifically replaced "hearing" with "meeting" in the body of the section, and the heading of a section cannot change the language of the section. See Ord. 118012 § 75 (1996); State v. T.A.W., 144 Wn. App. 22, 26, 186 P.3d 1076 (2008) ("While such labels are meant to be helpful, they cannot change the meaning of the statute in question."). The "record" in that heading is simply the electronic recording made of what was said at the meeting; it is not "the record" because it refers to no documentary evidence or decisions.

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recommendation is "essentially *de novo*" because it is based on "evidence in the record before the Examiner." Id., Concl. 3. For the reasons stated above, that is an accurate reading of the Code.

c. The burden of proof is solely on the appellant; it does not shift.

The Owner invents a shifting burden of proof that does not exist. The Code is clear that the burden remains on the appellant: "The appellant bears the burden of proving that the Board's recommendation should be rejected or modified." SMC 25.12.560.B. Nevertheless, the Owner maintains that "this burden only arises after the Board has presented a recommendation that has prima facie support" based on some record created in front of the Board, not the Examiner. Opening Brief at 17. The Owner is incorrect legally and practically.

As a legal matter, the only time that the Examiner employs a shifting burden is where the Code provides no burden of proof. "Where the applicable law does not provide that the appellant has the burden of proof, the Department must make a *prima facie* showing that its decision or action complies with the law authorizing the decision or action." Hrg. Ex. Rule 3.17(c). The Examiner has long applied that rule to Board decisions on certificates of approval, for which the Code provides no burden of proof. See, e.g., In re Garfield High School, LP-05-001, Findings and Decision at Concl. 4 (Nov. 14, 2005); In re Latona School, LP-95-002, Findings and Decision at Concl. 4 (May 13, 1996). Here, by contrast, the Code provides the burden of proof, which the Examiner must apply: "Where the applicable law provides that the appellant has the burden of proof, the appellant must show by the applicable standard of proof that the Department's decision or action does not comply with the law authorizing the decision or action." Hrg. Ex. Rule 3.17(b).

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The law makes sense as a practical matter. If the Owner were right, the Board would have to hire outside experts to undertake a formal financial impact analysis before its meeting on recommended controls. Because such analyses are likely to be complicated and contentious, the volunteer Board would need to provide for conflicting testimony and documentary evidence at its meeting, and would need to document how a majority of the Board resolved the conflicting evidence. This would be a costly yet necessary step in every single controls recommendation under the Owner's reading of the Code. Because an owner could raise "no reasonable economic return" for the first time before the Examiner, the Board would need to conduct the formal analysis even if the owner made no mention of such a claim before the Board's meeting, all to avoid losing automatically in front of the Examiner for failure to make a *prima facie* case on the basis of the Board's record.

Thankfully, the Code sensibly avoids the inefficient process invented by the Owner. Although a property owner is free to put expert testimony in front of the Board, the Board only needs to decide whether it is convinced by that testimony. Only if a property owner appeals the Board's recommendation does either side have to load up with experts and attorneys to focus on the one hearing that creates the record on which the Examiner is to base her decision—one on which the appellant carries the sole burden of proof.

d. The Owner did not establish what factors the Board considered when assessing reasonable economic return, and that fact would be immaterial to the Examiner's decision in any event.

The Owner misses the mark when complaining about the Examiner allegedly condoning the Board's use of impermissible factors. As a factual matter, the Owner presented the Examiner no evidence beyond the hearsay testimony of Mr. Nimmer to establish what factors individual Board members considered, let alone what the Board, as such, considered. Accord F&R, Concl.

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5 ("the Owner did not establish what factors the Board considered"). Repetition of the allegation in the Owner's opening brief does not add any credence to it.

As a legal matter, the factors considered by the Board are irrelevant. The standard is not "arbitrary and capricious."[7] The Examiner correctly observed that "the issue before the Examiner is not what the Board considered but whether the Board's recommended controls and incentives are supported by substantial evidence in the record before the Examiner." F&R, Concl. 5. The burden remained on the Owner to present evidence to the Examiner sufficient to convince her that, in light of the relevant factors, the Board's recommendation should be rejected because imposition of the proposed controls would leave the Owner with no reasonable economic return.

IV. CONCLUSION

Because the Owner has not sustained its burden of proving that the Examiner's recommendation should be rejected, the Department respectfully asks the Council to affirm the Examiner's recommendation and enact an ordinance containing the recommended C&I. See SMC 25.12.630.C, and .640.B.1.

Respectfully submitted November 22, 2010.

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[7] Under the "arbitrary and capricious" standard, the court focuses on the process to determine whether it was a "process of reason." Rios v. Washington State Dept. of Labor & Industries, 145 Wn.2d 483, 501, 39 P.3d 961 (2002). By contrast, the "substantial evidence" standard applicable here focuses on the substance of the decision and whether facts support it, regardless of how the decision was reached.

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CERTIFICATE OF SERVICE

I certify that, on this date, I sent a copy of this document to the following parties in the manner indicated below:

City Clerk
Attention: Sally J. Clark
c/o Ketil Freeman
Seattle City Council
600 – 4th Ave., Floor 3
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Hand delivery

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the foregoing being the last known addresses of the above-named parties.

DATED this 22nd day of November, 2010, at Seattle, Washington.

Rosie Lee Hailey

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FINDINGS AND RECOMMENDATION
OF THE HEARING EXAMINER FOR THE CITY OF SEATTLE

In the Matter of Controls and Incentives for

THE EITEL BUILDING
1501 Second Avenue

Hearing Examiner File:
LP-10-001

Board File:
22/10

Introduction

The Landmarks Preservation Board issued a recommendation on controls and incentives for the Eitel Building, located at 1501 Second Avenue, and the property owner timely filed an objection to the recommendation. The matter was heard before the Hearing Examiner on April 13, 14, and 15, and May 12, 2010. Parties represented at the hearing were the property owner, 1507 Group LLC (Owner), by Lawrence A. Costich and Curtis R. Smelser, attorneys-at-law; and the Landmarks Preservation Board (Board), by Roger D. Wynne, Assistant City Attorney. The Examiner visited the property, and the record was held open through May 28, 2010 for post-hearing filings.

For purposes of this recommendation, all section numbers refer to the Seattle Municipal Code, as amended, (SMC or Code) unless otherwise indicated. Having considered the evidence in the record and inspected the site, the Examiner enters the following findings of fact, conclusions and recommendation on controls and incentives.

Findings of Fact

1. The subject property is known as the Eitel Building (building) and is addressed as 1501 Second Avenue. It is located on the northwest corner of the intersection of Second Avenue and Pike Street, within the central business district and two blocks east of the Pike Place Market. It abuts the 38-story Opus condominium tower on the north and is bordered on the west by an alley that runs parallel to Second Avenue. Across the alley is the two-story Liberty Building.

2. The building is a seven-story rectangular structure with tan-colored brick cladding and terra-cotta ornamentation. Six stories were built in 1904 of unreinforced masonry with a steel column and lintel base support system on the southern and eastern sides, and an interior steel column and girder system supporting wood floor and roof framing. The seventh story was added in 1906. The southern and eastern façades are considered primary. Exhibit 26.

3. The building covers most of the 5,592-square-foot site and is approximately 90 feet tall. The basement extends partially under the adjoining sidewalk, and there is a light well that begins with the second floor on the western elevation.

APPENDIX A

4. The Owner purchased the building in 1975 as an investment in the hope that future renovation would be possible. When renovation to building code standards proved too costly, the Owner rented out the ground floor to commercial tenants and has kept the upper six floors vacant. The Owner also leases out billboard space on the west exterior of the building. Over the years, deterioration and earthquake damage have required structural work to stabilize the building.

5. Until recently, the zoning on the property was DMC (Downtown Mixed Commercial) 240, which would have allowed construction of a 240-foot building. However, in 2004, the Owner obtained a permit to renovate the building within the existing shell. Although the renovations proved too costly for the Owner to proceed, the building permit has been repeatedly renewed and remains active.

6. In 2006, the Owner learned that the property would be rezoned to its present zoning, DMC 240/290-400. The Owner determined that the new zoning would allow one property on the block to be developed to a height of 400 feet but would limit other development on the same block to a maximum height of 160 feet. The Opus tower to the north was to be constructed to approximately 400 feet. Therefore, the Owner decided to construct a 240-foot building on the subject property before the new zoning took effect.

7. The Owner hired an architect, who developed plans for a 22-story building with 92 residential units above 23,000 square feet of administrative office space and 3000 square feet of retail space. The proposal, which included demolition of the existing building, was reviewed in a meeting with the Design Review Board in February of 2006. Exhibit 18.

8. In August of 2006, the Landmarks Preservation Board (Board) designated the building as a landmark following nomination by Historic Seattle. The Board determined that the building "embodies the distinctive visible characteristics of an architectural style, period, or of a method of construction." *See* "Staff's Recommendation on Controls and Incentives" (January 13, 2010) attached to January 26, 2010 letter from Karen Gordon to the Hearing Examiner (Staff's Recommendation). The Owner then retained counsel to negotiate with the Board on a Controls and Incentives Agreement for the building.

9. Following designation, the Owner revised the development proposal for the site to remove the seventh floor and add a 16-story tower above the existing six-story building, preserving the south and east façades. The building would be 16 floors of residential above one level of retail use and five floors of office use. *See* Exhibit 29. The Design Review Board met to consider the revised proposal in October of 2006. Exhibit 19.

10. In January of 2007, the Owner filed a Master Use Permit (MUP) application, thereby vesting to the then-existing 240-foot zoning. At the same time, the Owner submitted the MUP drawings and a project description to the Board's staff and asked to schedule a meeting with the Board's Architectural Review Committee (ARC). Exhibit 27.

11. The ARC is a subcommittee of the Board composed of members with architectural expertise. The ARC is available to meet with an owner to review a proposal, and provide feedback and suggestions on it, before the owner seeks a Certificate of approval from the full Board. The process is collaborative, and the goal is to achieve a design solution that meets both the owner's needs and the Board's goal of preserving the designated historic features. Testimony of Sarah Sodt, 4/15/10 at 1:22. *See* SMC 25.12.750 (reproduced below).

12. A certificate of approval is required from the Board before the owner of a designated landmark may alter or significantly change the designated features or characteristics of the landmark. *See* SMC 25.12.080, .670.

13. The Board's coordinator testified that the Board has granted certificates of approval that resulted in the destruction of some designated features of landmark buildings when the aspects of the buildings that remained were sufficient to convey their historical importance. The coordinator cited two recent examples: the Pacific McKay Ford Building on Westlake Avenue, where the primary façades were removed and are in storage for future installation on a new development; and the Terminal Sales Annex Building at 1931 Second Avenue, a narrow building for which the Board approved retention of the street-facing façade and the addition of a multi-story tower atop the landmark. Testimony of Sarah Sodt, 4/15/10 at 1:22-1:26 and 2:20. She did not know of any certificate of approval application for construction of additional stories atop a landmark that has been denied. Testimony of Sarah Sodt, 4/15/10 at 2:22.

14. It is not necessary for controls and incentives for a building to be in place before an owner seeks a certificate of approval for proposed changes to it. Testimony of Sarah Sodt, 4/15/10 at 1:18.

15. Working with an architect not known to have experience with historical structures, the Owner presented the MUP proposal to the ARC in March of 2007. The ARC suggested that the architect consider an alternative that reduced the tower height and explore a tower setback. The ARC did not state that the design needed to stay within the existing shell of the building. Testimony of Sarah Sodt, 4/15/10 at 1:28-130.

16. To determine the economic impact that might result from controls and incentives that could be adopted for the building, the Owner retained an appraiser to evaluate the feasibility of three development scenarios. The first appraisal was produced on June 8, 2007. The three development scenarios evaluated were office and retail, residential condominium and retail, and residential apartment and retail. They were based on the renovation plans developed for the 2004 building permit. Thus, for each scenario, the appraiser assumed that forthcoming controls and incentives for the building would limit construction to the building's existing shell. *See* Tab 2 to Exhibit 1[1] at 211, 279, 289 and

[1] Tab 2 to Exhibit 1 consists of bound documents, the content of which is essentially the same as the compact disc included under Tab 2 of Exhibit 1. The page numbers referenced in Exhibit 1 and Tab 2 to Exhibit 1 are the Bates-stamped numbers at the bottom of the pages.

299. The appraiser concluded that none of the three development scenarios would be "expected to produce a sufficient return on investment necessary to attract capital to the project." Tab 2 to Exhibit 1 at 193.

17. Under the caption, "Extraordinary Assumptions and Limiting Conditions," the 2007 appraisal notes that the three development scenarios considered "are believed to reflect reasonable and realistic use constraints" that may be imposed on the property through the controls and incentives process. The appraiser reserves the right to modify the appraisal's conclusions if "any or all of the ... assumptions utilized prove to be in error." Tab 2 to Exhibit 1 at 211.

18. The Owner chose not to return to the ARC with a revised design proposal and, instead, filed an application for a certificate of approval in October for essentially the same proposal the ARC had reviewed in March. Exhibits 28 and 29. On November 5, 2007, the Board's staff sent the Owner an application checklist showing which pieces of the certificate of approval application were still missing.

19. On November 15, 2007, as part of the MUP process, the Director of the Department of Planning and Development (DPD) issued a SEPA determination of significance, requiring that an environmental impact statement be prepared to analyze the proposal's historic preservation and land use impacts. Exhibit 22. The Owner retained an environmental consultant to begin work on the EIS. Testimony of Richard Nimmer, 4/13/10 at 10:33.

20. On May 7, 2008, the Owner's appraiser issued an updated appraisal to evaluate the likely economic impact of controls that might be imposed on the building. Tab 2 to Exhibit 1 at 144. Again, the appraisal assumed that any of the three development scenarios would involve "essentially 'rebuilding' the existing seven-story improvement and, in addition, foregoing the opportunity to develop the site to the full extent of the remaining 15 stories." Tab 2 to Exhibit 1 at 172. Under these assumptions, the appraiser again concluded that none of the three scenarios would be capable of producing a sufficient return on investment to attract capital. Tab 2 to Exhibit 1 at 172.

21. The 2008 appraisal also considered the feasibility of the 22-story revised MUP proposal, including demolition of the building, for residential condominium use and residential apartment use. Assuming a minimum rate of return required to attract capital of 75 percent, the appraisal concluded that both of these development scenarios would be feasible. *See* Tab 2 to Exhibit 1 at 169, and 174-76.

22. The Owner believes that as a result of the landmark designation, the building is capped at 90 feet with the exception of a possible small "penthouse" addition. Testimony of Richard Nimmer, 4/13/10 at 10:30. However, the Owner acknowledged that if controls on the building did not prevent an increase in building height, the air rights above the building would be valuable to the owners of adjacent buildings. As an alternative to a tower atop the existing building, the Owner agreed that the air rights could be sold to help fund renovation of the existing building. Testimony of Richard

Nimmer, 4/13/10 at 11:18. The Owner's appraiser agreed that a purchase of air rights could make building renovation possible. Testimony of Brian O'Connor, 4/14/10 at 11:54.

23. On May 9, 2008, the Owner submitted the 2007 and 2008 appraisals to the Board, together with a letter from the Owner's architect, indicating that the application now included demolition of the building, and other materials required to complete the October 2007 certificate of approval application. Exhibit 31.

24. On April 22, 2009, the Owner inquired of DPD concerning the ramifications of placing the revised MUP application on hold while continuing to pursue a certificate of approval from the Board. DPD responded on May 8, 2009, that the Owner would need to terminate the certificate of approval process in order to remove the MUP from active status. Exhibit 24.

25. On May 14, 2009, the Owner notified the Board that it was withdrawing its application for a certificate of approval to demolish the building. Exhibit 25.

26. The Owner and Board continued to discuss controls and incentives for the building. On January 12, 2010, the Owner declared that the negotiations were at an impasse.

27. On January 20, 2010, the Board adopted recommended controls and incentives, which were forwarded to the Hearing Examiner on January 26, 2010. The recommended controls and incentives require that the Owner obtain a certificate of approval from the Board before making alterations or significant changes to the exterior of the building with the exception of the light well on the western elevation. *See* Staff's Recommendation.

28. The Owner timely filed a statement of objections to the Board's recommended controls and incentives. The objections state that the recommended controls are not supported by applicable law and substantial evidence in the record; prevent the owner from realizing a reasonable return on the site; resulted from consideration of factors other than, and in addition to the factors listed in SMC 25.12.590 for determining a reasonable return on the site; deprive the owner of a reasonable economic use of the site; and deny the Owner substantive due process and amount to an inverse condemnation (taking) of the site, in violation of the constitution.

29. In preparation for the hearing on the Owner's objections to the Board's recommended controls and incentives, the Owner's appraiser issued a March 30, 2010 summary appraisal of the property that updated information on its market value. Exhibit 1, Tab 11 at 489. The appraiser determined that the "highest and best use" of the property was to "hold for future development" and valued it at $2,500,000 under the "vested MUP" proposal, and $1,650,000 under the existing 160-foot zoning assuming that no controls were imposed. Exhibit 1, Tab 11 at 493, 582 and 587.

30. On April 7, 2010, the Owner's appraiser issued an updated appraisal to evaluate the economic impact of the imposition of controls on the property. Exhibit 1, Tab 12 at 603.

The appraiser again assumed that the Owner would be required to preserve the existing shell of the building other than the light well. Exhibit 1, Tab 12 at 626. And the appraiser again reserved the right to modify the conclusions in the report should the assumption on controls be proven incorrect. Exhibit 1, Tab 12 at 626. As in the earlier appraisals, the appraiser concluded that "rehabilitation of the existing improvements is not considered to be feasible" under the assumed controls. Exhibit 1, Tab 12 at 605.

Applicable Law

31. SMC 25.12.570 provides that "[o] n the basis of all the evidence presented at hearing," the Examiner is to determine whether to recommend that the proposed controls and incentives recommended by the Board be accepted, rejected or modified. Further, the Examiner "shall not recommend any control which is inconsistent with any provision of this chapter, or which requires that the ... [landmark] be devoted to a particular use," or that imposes any use restriction, control or incentive if the effect, alone or in combination, "would be to prevent the owner from realizing a reasonable return on the [landmark]." SMC 25.12.590 lists the factors to be considered in determining a reasonable return on the landmark.

32. SMC 25.12.580 states that "in no event shall ... any proceedings under or application of this chapter deprive any owner of a ... [landmark] of a reasonable economic use of such ... [landmark]."

33. SMC 25.12.750 lists the factors that the Board and Examiner are to take into account in considering an application for a certificate of approval. The factors relevant to this case are the following:

> A. The extent to which the proposed alteration or significant change would adversely affect the specific ... [landmarked] features or characteristics...;
>
> B. The reasonableness or lack thereof of the proposed alteration or significant change in light of other alternatives available to achieve the objectives of the owner and the applicant;
>
> C. The extent to which the proposed alteration or significant change may be necessary to meet the requirements of any other state law, statute, regulation, code or ordinance; [and]
>
> D. Where the Hearing Examiner has made a decision on controls and economic incentives, the extent to which the proposed alteration or significant change is necessary or appropriate to achieving for the owner or applicant a reasonable return on the ... [landmark], taking into consideration the factors specified in Sections 25.12.570 through 25.12.600 and the economic consequences of denial; provided that, in considering the factors specified in Section 25.12.590 for purpose of this subsection, reference to the times before or after the imposition of controls

shall be deemed to apply to times before or after the grant or denial of a certificate of approval;

....

Conclusions

1. The Hearing Examiner has jurisdiction over this matter pursuant to SMC 25.12.540.

2. The Owner's constitutional issues of inverse condemnation and substantive due process are beyond the jurisdiction of a quasi-judicial body, and the Examiner has not considered them. *See Yakima Cy. Clean Air Authority v. Glascam Builders, Inc.*, 85 Wn.2d 255, 257, 534 P.2d 33 (1975).

3. Under the scheme of Subchapter V. of Chapter 25.12 SMC, the Hearing Examiner's recommendation on controls and incentives is essentially *de novo*. The issue before the Examiner under SMC 25.12.560.B is whether the Board's recommended controls and incentives are supported by substantial evidence in the record before the Examiner. "Under the substantial evidence standard, there must be a sufficient quantum of evidence in the record to persuade a reasonable person that the declared premise is true." *Wenatchee Sportsmen Ass'n v. Chelan Cy.*141 Wn.2d 169, 176, 4 P.3d 123 (2000) (citations omitted). The "appellant bears the burden of proving that the Board's recommendation should be rejected or modified." SMC 25.12.560.B. The "appellant" in this case is the Owner.

4. The Owner objects to the Board's recommendation as not being supported by applicable law and substantial evidence in the record before the Board. As noted, however, the Examiner's review under the Code is *de novo*. Therefore, the record before the Board is immaterial in this proceeding.

5. The Owner asserts that the Board erroneously considered factors other than, and in addition to the exclusive factors listed in SMC 25.12.590 for determining a reasonable return on the site. However, the Owner did not establish what factors the Board considered in reaching its recommendation on controls and incentives. Moreover, the issue before the Examiner is not what the Board considered but whether the Board's recommended controls and incentives are supported by substantial evidence in the record before the Examiner.

6. The Owner's entire case, including all the work of the Owner's appraiser, rests on the premise that the Board's recommended controls would limit any development of the property to the shell of the existing building. Yet there is no evidence in record to support that premise.

7. The recommended controls require only that the Owner obtain a certificate of approval from the Board before making exterior alterations to the building, with the exception of eliminating the light well. Both the evidence in the record and the

applicable law demonstrate that the certificate of approval process is a collaborative one, designed to achieve both the owner's and City's needs with respect to the landmark.

8. The Owner argues that the addition of floors to the building would "significantly change and adversely affect" the features or characteristics specified in the designation, and that it is not clear the Board would approve such a change. However, the certificate of approval process exists to examine and, if possible, resolve such challenges. The ARC works with the owner toward development of alternative designs. The Board considers several factors, including the reasonableness of the proposed alteration in light of the alternatives available to achieve the owner's objectives. *See* SMC 25.12.750.B (Finding 33). The Code does not dictate a particular outcome, nor does it require preservation of all designated historic features. Moreover, past Board practice, including this Owner's experience with the ARC, demonstrates that approval of a tower above the landmark is in no way foreclosed.

9. The Owner states that if the Board had believed additional height was acceptable, it would have said so in its recommendation, as it did with the exception allowing infill of the light well. The Board is not a legislative body, and it is not clear that the rules of statutory construction apply to its recommendation. In any event, the fact that the Board did not include an exception for additional height above the landmark does not indicate that additional height is precluded; rather, it suggests that the addition of floors above the landmark would require the exploration of alternatives that is an inherent part of the certificate of approval process.

10. The Owner correctly asserts that the evidence fails to demonstrate that adding floors to the building could be accomplished and would provide the Owner a reasonable rate of return. The evidence does show that from 2006 through 2007, the Owner pursued the original 22-story MUP proposal that included preservation of the south and east façades and construction of a tower above the existing landmark. Working with an architect not known to have experience with historical structures, the Owner met with the Design Review Board and the ARC on the MUP proposal. Both bodies asked for revised alternatives, although for slightly different reasons. The evidence shows that in 2008, the Owner received an appraisal that indicated demolition of the landmark and sale of the property for construction of a 240-foot or 160-foot tower would result in a rate of return necessary to attract capital to the project. The evidence also shows that in 2008, the Owner decided to demolish the building and terminated the certificate of approval process. During the intervening two years, the Owner has directed resources toward convincing the Board that any controls and incentives placed on the landmark would prevent the Owner from realizing a reasonable return and deprive the Owner of a reasonable economic use. As a result, we do not know with certainty whether a tower can be built atop the landmark, and there is no evidence in the record on whether development available to the Owner through the MUP and certificate of approval processes would provide the Owner with a reasonable return and a reasonable economic use. The Board's recommended controls and incentives would afford the opportunity for development of the information necessary to make those determinations. *See* SMC 25.12.750.D (Finding 33).

11. The Owner drew an analogy between this case and In re Bon Marche Stables, LP-08-004, which also involved an owner's challenge to the imposition of controls and incentives that required a certificate of approval for exterior alterations. In that case, however, the Board did not dispute that the imposition of controls and incentives would limit future development to the shell of the existing building.

12. Because all of the Owner's evidence is based on an invalid assumption, the Owner has not met the burden of proving that the Board's recommended controls and incentives should be rejected or modified.

Recommendation

The Hearing Examiner recommends that the City Council accept the Board's recommendation on controls and incentives for the Eitel Building.

Entered this 9th day of June, 2010.

Sue A. Tanner
Hearing Examiner

Concerning Further Review

NOTE: It is the responsibility of the person seeking further review of a Hearing Examiner recommendation to consult appropriate Code sections to determine applicable rights and responsibilities.

SMC 25.12.620 provides as follows:

> Any party of record before the Hearing Examiner may appeal the recommendations of the Hearing Examiner regarding controls and incentives to the Council by filing with the City Clerk and serving on all other parties of record a written notice of appeal within fourteen (14) days after the Hearing Examiner's decision is served on the party appealing.

Department's Response Brief, APPENDIX B

The Department asks the Council to affirm the Examiner's recommended controls and incentives ("C&I") on the grounds articulated by the Examiner:

> *The Owner's entire case, including all the work of the Owner's appraiser, rests on the premise that the Board's recommended controls would limit any development of the property to the shell of the existing Building. Yet there is no evidence in the record to support that premise....*
>
> *Because all of the Owner's evidence is based on an invalid assumption, the Owner has not met the burden of proving that the Board's recommended controls and incentives should be rejected or modified."*

F&R, Concl. 6, 12. The Council therefore should follow the lead of the Examiner and not delve into the record of the debate over whether the Owner would be deprived of a reasonable economic return or use, even assuming incorrectly that the Owner were limited to the existing shell of the Building.

Nevertheless, as stated in the Department's Response Brief, the Department does not want to leave the Council with the misimpression that the Department did not engage in that debate (as the Owner's opening brief seems to suggest) or even lost that debate. The Department is therefore providing the Council with the following text, which is lifted directly from the Department's Post-Hearing Brief to the Examiner. In this text, the Department spells out why the Owner failed to carry its burden, even if the Owner's false assumption were granted.

*Again, **the Council does not need to review this text**. The Department provides it only in case the Council deems it informative.*

A. Even assuming incorrectly that the C&I would limit future development to the existing shell, the Owner has not sustained its burden of proving that it would be left with no reasonable economic return or reasonable economic use.

The Department respectfully submits that the Examiner should end her decision by concluding that the Owner cannot sustain its burden using the false assumption that the mere imposition of the recommended C&I would necessarily limit future development to within the shell of the existing building. The Department's proposed findings and conclusions are limited to that basis for affirming the recommended C&I. Going any further would be to engage in *dicta*.

However, in an abundance of caution and at the expense of greatly expanding the briefing, the Department offers an alternative basis for affirming the recommended C&I: even granting the false assumption that imposition of the C&I would limit development to within the

existing shell, the Owner has still not sustained its burden of proving that the Owner would be prevented from realizing a reasonable return or be deprived of a reasonable economic use.

1. The Owner cannot sustain its burden of demonstrating no reasonable economic return by omitting one factor, spinning past and future expected annual returns, and relying on questionable analyses of market value.

The five exclusive factors for assessing "reasonable return" are set forth in SMC 25.12.590. For purposes of this case, they may be grouped under four categories. The Owner has not sustained its burden under any of these categories, even assuming incorrectly that the C&I would limit future development to the existing building shell.

a. The Owner did not address the return on comparable buildings not subject to similar C&I. (SMC 25.12.590.E.)

One factor is "[t]he net return and rate of return realized on comparable sites not subject to controls imposed pursuant to this chapter." SMC 25.12.590.E. Mr. O'Connor did not address this factor, so it cannot be used to sustain the Owner's burden of proof.

Perhaps without realizing how readily it could apply to Mr. O'Connor, the Owner's rebuttal expert, Mr. Gibbons, criticized the Department's expert for not addressing the net return on the Eitel Building site in relation to returns on sites not subject to controls. Rec. 4/15 at 5:07 - 5:08. If that is indeed a valid reason for attacking the Department's expert (whose goal was simply to mirror a portion of Mr. O'Connor's analysis, albeit with different input assumptions), it must be an even more powerful indictment of Mr. O'Connor's work.

b. The Owner has realized steady net income—on average more than $160,000, or nearly 12% of the assessed value—over the past five years. (SMC 25.12.590.B.)

Another factor relevant to "reasonable return" is "[t]he owner's yearly net return...during the five (5) years prior to the imposition of specific controls and/or incentives." SMC 25.12.590.B. The Owner's net income over the past five years has been steady, notwithstanding Mr. O'Connor's attempts to manipulate the numbers.

Mr. O'Connor listed actual gross income and gross operating expenses for the past five years. Ex. 1, Tab 12 at 708. Mr. O'Connor deducted an "Opus Payment" of $80,000 from 2006 gross income. Mr. O'Connor somehow justified that deduction as an anomaly, yet simultaneously justified including as an "operating" expense the legal and accounting fees generated "largely as a result of the owner's attempt to comply with the City's historic preservation requirements." Ex. 1, Tab 12 at 707. Setting aside the characterization of the Owner's attempts to oppose imposition of C&I as an attempt to comply with City requirements, the fact remains that those expenses are not properly deemed "operating" expenses for purposes of calculating "net return." Mr. Shorett testified that those expenses were included improperly, and the Owner's rebuttal witnesses offered nothing to challenge that testimony.

Even if one were to accept the omission of the Opus payment as income, if one were to properly omit the legal and accounting charges as expenses, the result would show an average net return of over $163,000, with no discernible trend:

	2005	2006	2007	2008	2009	Avg.
Reported Net Operating Inc.	164,340	86,865	(19,722)	132,679	107,664	94,365
Add Reported Legal & Acctg.	450	56,901	145,079	77,162	67,420	
Actual Net Operating Inc.	164,790	143,766	125,357	209,841	175,084	163,768

See Ex. 1, Tab 12 at 708.

Although otherwise adhering to the approach used in Bon Marche Stables, which reported the past five years "net return" as a simple matter of net income, see Conclusion 11, Mr. O'Connor felt compelled—perhaps because the net return for the Eitel Building is actually robust—to report the net return figure as a percentage of the assessed value of the property. Ex. 1, Tab 12 at 708. Again, though, even if one accepts the omission of the Opus payment, if one properly omits the legal and accounting charges, the average return against assessed value is nearly 12%:

	2005	2006	2007	2008	2009	Avg.
Assessed Value ("AV")	951,600	951,600	1,717,800	1,958,200	2,237,800	
Reported Return Against AV	17.3%	9.1%	-1.1%	6.8%	4.8%	7.4%
Actual Return Against AV	17.3%	15.1%	7.3%	10.7%	7.8%	11.7%

See Ex. 1, Tab 12 at 708.

The Owner, who owns the property free and clear, is therefore realizing a steady net return on the income generated from the rent of the first two floors, despite needing to make moderate investments to maintain the shell of the upper portion of the structure. This makes sense: if you own an asset in a prime location, you should expect to generate reasonable revenue from the ground floors while doing the minimum necessary to support the upper floors.

Mr. O'Connor's final attempt to run from these numbers should be rejected. "To provide somewhat more useful context," he offered a calculation of some "internal rate of return" based on a hypothetical past sale, with and without some imagined past imposition of controls. Ex. 1, Tab 12 at 708-09. As evidence that not even Mr. O'Connor deems this relevant to a straight-forward calculation of actual net return, note that he did not employ this "internal rate of return" calculation in his only prior analysis of past yearly returns. See Ex. 2 to Ex. 1 at 171.

c. With or without imposition of C&I, the likely future net yearly return would be 11% of the current market value. (SMC 25.12.590.C.)

Another factor relevant to "reasonable return" consists of "[e]stimates of the owner's future net yearly return...with and without the imposition of proposed specific controls and/or incentives." SMC 25.12.590.C. With or without the imposition of the recommended C&I, the

highest and best use of the Eitel Building would be to maintain it in its current state. This was Mr. O'Connor's conclusion: even assuming no C&I, current market conditions would not be favorable to undertaking a new development on the site. Ex. 1, Tab 11 at 505.

The only reasonable estimate of the Owner's future net yearly return is therefore an extension of the past five years net yearly return of approximately $160,000 (or an average of nearly 12% of the assessed value of the property). This is consistent with Bon Marche Stables, which concluded that "[t]he continued use of the property in its current state would be expected to return an amount that would be equivalent to the net annual income...." Conclusion 12. Bon Marche Stables took that figure a step further: it reported the most recent past year's net annual income as a percentage of the property's pre-C&I market value.[8] Id. Using that same approach, the expected future net yearly return on the Eitel Building would be 11% of the $1,650,000 pre-C&I market value calculated by Mr. O'Connor.[9]

Rather than adhere to his own advice (that the highest and best use is to hold the property in its current state) and the approach in Bon Marche Stables, Mr. O'Connor tried to spin the "future net yearly return" factor into something negative. He first descended into unsupported fantasy: he assumed that a buyer would pay the Owner $1,650,000 for the building and would then, rather than continue to enjoy existing annual income of 11% of that price, would spend over $14,000,000 creating market-rate apartments that would result in a certain loss in today's market. Ex. 1, Tab 12 at 701. From that fantastic assumption, he reported a yearly net return on equity of -26.8%. Id. at 705. Mr. O'Connor admitted in testimony that he provided no support for that figure, leaving neither the Examiner nor the Department able to assess his formula or his calculation of that figure—this despite both Mr. O'Connor's and Mr. Gibbons's criticism of Mr. Shorett for allegedly not showing all of his calculations.

To complete his spin, Mr. O'Connor suggested that operating expenses will necessarily increase to meet the demands of some sort of new and different deterioration. As evidence, he reported that "the deteriorated condition of the improvements has prompted the City of Seattle to threaten condemnation of the improvements...." Ex. 1, Tab 12 at 707. Testimony from Mr. Nimmer and others demonstrated the falsity of that statement—the City has not sought to condemn the Eitel Building over the last 35 years. Mr. O'Connor was unable to offer any fact in his testimony to support his prediction that expenses would increase to address deterioration. There is no evidence that the seismic work performed in 2001 and 2006 did not stabilize the portions of the building that had been compromised by the Nisqually earthquake. See Ex. 2 to Ex. 1 at 451; Rec. 4/14 at 1:36 – 1:40. The record shows only that the Owner has undertaken minimal necessary maintenance on the upper floors over the past 35 years; there is nothing to suggest that the building is poised for a quantum leap, or even an upward creep, in capital or maintenance expenses.

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[8] The decision reports a figure of 3.75%, which is the result of the $88,000 annual income for the most recent year (2007) reported in Conclusion 11, divided by the $2,345,000 "before" market value reported in Conclusion 5.

[9] This is the result of the $175,084 actual net operating income for the most recent year (2009), see *infra*, divided by the $1,650,000 "before" market value reported by Mr. O'Connor. See Ex. 1, Tab 12 at 705.

d. Mr. O'Connor's approach to analyzing the "after" value is not credible. (SMC 25.12.590.A, .D.)

Another "reasonable return" factor is the market value of the property before imposition of C&I. SMC 25.12.590.A. This is relevant because it is possible that property may already be of little value, such that there is little impact from imposing C&I. Contrary to Mr. O'Connor's stated belief, the Code does not establish the "before" value as the baseline below which value may not fall. If he were correct, there would scarcely be any landmark preservation in the City. One must start and end with the likelihood that imposition of C&I—as with any constraint imposed on a specific parcel—will lower the market value of property to some extent. Accord Ex. 1, Tab 12 at 706 (Mr. O'Connor's quote of a treatise about the "inevitable" effect of imposing a restraint on property use). Assessing the "before" value involves the relatively conventional "sales comparison" method. See SMC 25.12.590.A. Here, Mr. O'Connor concluded that the value of the Eitel Building before imposition of C&I is $1,650,000.

To determine whether imposition of C&I leaves the owner with a reasonable return, the Code also requires consideration of the market value of the property after imposition of the C&I. SMC 25.12.590.A. Part of that involves assessing the net return and the rate of return necessary to attract capital for investment after the imposition of C&I. SMC 25.12.590.D. Mr. O'Connor assessed the "after" value through "feasibility analysis/development approach" methodology, which views the property from the perspective of a potential buyer/developer. See generally Ex. 1, Tab 12 at 700, 702. It begins by asking whether it would be feasible for a buyer to pay the owner the "before" land value and still develop the property in a way that yields returns sufficient to attract capital. If paying the owner the "before" land value would yield an infeasible project, the methodology then involves lowering the purchase price until it would be possible for the buyer to undertake a feasible development. That lowered purchase price is the "after" value of the property.

As described in the following subsections, Mr. O'Connor's approach to the "after" value is not credible because: (1) the Owner is taking actions inconsistent with Mr. O'Connor's conclusion that there would be only a negative "after" value; (2) Mr. O'Connor's 2007 data demonstrated that a feasible market-rate project, with a positive purchase price for the Owner, was possible; (3) Mr. O'Connor has employed shifting assumptions and methodology that consistently favor a conclusion of negative "after" value; and (4) Mr. O'Connor has consistently disregarded elements of value to a renovation scenario, most crucially the value of low-income housing tax credits.

(1) By continuing to renew the building permit for renovation of the building, the Owner demonstrates a lack of confidence in Mr. O'Connor's conclusion that renovation of the Eitel Building is infeasible.

Mr. O'Connor's conclusion that renovation of the building is infeasible runs headlong into the fact that the Owner is not convinced. Mr. O'Connor allowed in his testimony that, in light of his analyses, he believes no rational person would continue to maintain a building permit to renovate this building. Yet that is exactly what the Owner has done for years. Mr. Nimmer

anticipated that renovating the building for office use would make money when he initially pursued the project. He was not forced into that project—any suggestion that it was prompted by some condemnation threat (which never existed) or by the need to make the building structurally sound (which has been accomplished through targeted engineering projects) has been dispelled.

Why, then, does the Owner continue to keep the building permit alive, even after Mr. O'Connor has testified that doing so is irrational? It must be because maintaining the permit is, in fact, rational. Mr. Nimmer has been at this business for decades, at least long enough to learn that market forces ebb and flow. A rational, experienced real estate owner will see the value in being ready to time his or her jump into the market, especially without the delay of going through a new permitting process. Although the Owner must believe that Mr. O'Connor's methodology, assumptions, and conclusions have value in resisting the recommended C&I, the Owner will not take them to the bank. The Owner is voting with his feet—back to the DPD permitting counter again and again to be positioned to renovate the Eitel Building. If the Owner believed that Mr. O'Connor's conclusions were relevant in the real world—if he really believed that he could renovate the building only by losing millions of dollars—he would have torn up the building permit rather than continuing to renew it, most recently on the eve of the hearing in this case.

(2) Mr. O'Connor's 2007 data demonstrated that a feasible market-rate project, with a positive purchase price for the Owner, was possible.

Despite Mr. O'Connor's assertion that his calculations in 2007, 2008, and 2010 demonstrate that no renovation of the Eitel Building has ever made sense economically, see Ex. 1, Tab 12 at 606, his data disprove that assertion. Even taking at face value his cost assumptions in 2007, those data show that an apartment project would have been feasible at that time, albeit at a land sales price to the Owner less than the "before" value of the land. Cf. Ex. 2 to Ex. 1 at 202. As Mr. Shorett demonstrated, if Mr. O'Connor had only proceeded to the "development approach" portion of his methodology and had not thrown up his hands and declared victory after the "feasibility analysis," Mr. O'Connor would have found a positive "after" value. Ex. 14.[10] Mr. O'Connor offered nothing to rebut Mr. Shorett's conclusion.

(3) Mr. O'Connor's analysis is undermined by assumptions and methodology that shift in ways that favor a particular outcome.

Why did Mr. O'Connor not employ the "development approach" in 2007 even though, in 2008 and 2010, he correctly followed the "feasibility analysis" with the "development approach"? See Ex. 2 to Ex. 1 at 169-70 (2008); Ex. 1, Tab 12 at 702 (2010). This inconsistency is a symptom of a larger problem with Mr. O'Connor's work. Throughout his years-long involvement in this matter, his assumptions and methodology have shifted in ways that happen to assist the point the Owner would like Mr. O'Connor to substantiate. Whether

[10] Because Mr. O'Connor did not show how he derived certain figures in 2007, Mr. Shorett could not conclusively calculate that "after" value using Mr. O'Connor's methodology. See Ex. 14 at Line 19.

intentional or inadvertent, this pattern fatally undermines the reliability of Mr. O'Connor's conclusions.

Current market values vs. prospective market values. Mr. O'Connor conveniently flip-flopped on the question of whether to employ current market values or prospective market values. In 2007, he used current market values on the assumption that the renovation project was completed and stabilized as of the date of his report. Ex. 2 to Ex. 1 at 201. He explained: "Clearly, while such a condition is hypothetical in nature, it has been utilized, in this instance, as a means of minimizing potential forecasting error to a future date of completion and/or stabilization." Id.

He soundly rejected that approach in 2008—at the height of the apartment market when rents were soaring.[11] He dismissed his 2007 assumption as an "onus" and extolled the virtues and industry acceptance of assuming prospective values:

> The use of "prospective" valuation in the analysis is considered by many in the industry to more "realistically" reflect the potential financial performance of the development process, as it takes into account expected changes in rental rates, operating expenses, and pricing growth....
>
> .... The principal benefit of this approach is that the projection of future revenues, as needed to meet debt service and/or loan repayment obligations, may be more accurately estimated in keeping with market trends over a protracted development timeline.

Ex. 2 to Ex. 1 at 155-56. This new assumption just so happened to allow Mr. O'Connor to avoid using value numbers that might have favored one of the various renovation scenarios he analyzed.

Nevertheless, in 2010—now in the very trough of market values—Mr. O'Connor returned to his original assumption that allowed him to plug in rental values that currently make almost no development project in the City attractive. Ex. 1, Tab 12 at 626. The credibility of an appraiser's conclusions must be questioned when the appraiser rejects an assumption as an "onus" when doing so allows him to avoid high values, and then embraces that same assumption two years later so that he can employ values so low that they would make almost any development look infeasible.

Whether to analyze a range of renovation scenarios. By his own admission, Mr. O'Connor provided no data or documentation to support his decision to analyze only the apartment scenario as the "least infeasible" scenario in 2010. See Ex. 1, Tab 12 at 680-81. This stands in contrast to the approach he took in 2007 and 2008, where he provides analyses of office, apartment, and condominium scenarios. Compare Ex. 2 to Ex. 1 at 170, 202 with Ex. 1,

[11] Mr. O'Connor noted that, although a general slowing of the pricing for condominiums was evident in 2008, the market was then witnessing "[s]ubstantial rental rate growth and corresponding declines in [apartment] vacancy rates." Ex. 2 to Ex. 1 at 154.

Tab 12 at 701. When asked why he focused exclusively on the apartment scenario in 2010, he initially testified that the apartment scenario had been the least infeasible in his 2007 and 2008 analyses, but that proved incorrect: the 2008 analysis showed the office scenario to be the best performer. Ex. 2 to Ex. 1 at 170. If one horse had not consistently won the race in 2007 and 2008, Mr. O'Connor should have shown why he selected the horse he did in 2010. Because he did not, there is no way for the Department or the Examiner to assess Mr. O'Connor's selection of the apartment scenario as the "least infeasible."

In his criticism of Mr. Shorett, Mr. O'Connor spoke of the "red flags" that should go up when an appraiser does not show the data and calculations that support his conclusions. The absence of an analysis of the office and condominium scenarios from Mr. O'Connor's 2010 report is exactly such a "red flag."

Sudden use of an inflated construction cost estimate. Just because the Eitel Building has been allowed to dilapidate does not mean that the cost of renovation is prohibitive. The Owner's structural engineer, Mr. Lundeen, testified that the existing building permit design adequately addresses seismic issues; the Department's expert, Mr. Perbix, endorsed that view. The Owner relied on a 2001 cost estimate from Mr. Hendrickson to determine that pursuing an office renovation project (now manifest in the building permit) would be feasible. The Department's cost estimating expert, Mr. Stroming, endorsed Mr. Hendrickson's 2001 and later estimates, and added that he had seen buildings in worse shape that had been successfully renovated (naming the OK Hotel as an example). Mr. O'Connor used Mr. Hendrickson's estimates for his feasibility analyses in 2007 and 2008, even though he had been presented a much higher estimate from Ms. Matson. See Ex. 2 to Ex. 1 at 37. In short, until 2010, there had been roughly a decade of reliance on Mr. Hendrickson's cost estimates.

That all changed this year when Mr. O'Connor tossed aside Mr. Hendrickson's estimates in favor of Ms. Matson's recent, and significantly higher, estimate. As Mr. Stroming demonstrated, the difference in the three estimates—from Mr. Hendrickson, Mr. Stroming, and Ms. Matson—is not due to any appreciable difference in the types, amounts, or prices of the materials and labor needed to renovate the Eitel Building, but in the unreasonable contingencies larded into Ms. Matson's estimate. See Ex. 16. Mr. Stroming explained in detail how each of Ms. Matson's various contingencies was unreasonable, and especially why Mr. O'Connor incorrectly added a 5% developer's contingency on top of the 15% change-order contingency Ms. Matson already factored into her cost estimate.

The Owner put Mr. Hendrickson on the stand to rebut Mr. Stroming's testimony, but Mr. Hendrickson simply endorsed Mr. Stroming up and down, using terms like "I would agree with his conclusion" and "concur completely." The only point on which Mr. Hendrickson quibbled with Mr. Stroming was about the appropriate size of the construction contingency to be used for construction today, but Mr. Hendrickson readily conceded that in a more normalized market—a market in which development might make more sense generally—the construction contingency included by Mr. Stroming is appropriate.

Sudden resort to a contingency-laden cost estimate—one that adds millions of dollars to the cost of renovation—without good reason further undermines the reliability of Mr. O'Connor's conclusions.

Inflated and fluctuating sales and leasing cost assumptions. Mr. Shorett questioned why Mr. O'Connor included such an inflated sales and leasing figure as part of his project expenses. Mr. Shorett reported that "a sales and leasing commission for an apartment complex [is] typically a onetime lease-up cost that we estimate at $50,000." Ex. 10 at 3. The Owner's rebuttal witnesses, including Mr. O'Connor, did not challenge this statement.

Mr. O'Connor's sales and leasing figures were not only inflated, they varied wildly. In 2007, he included $385,000 for sales and leasing as a cost element in the apartment scenario—an amount equal to 2.5% of the project value he calculated. See Ex. 2 to Ex. 1 at 202. In 2008—at the height of the market, when a project was most likely to look feasible—he more than doubled that figure to $934,000, or 6.0% of project value. See Ex. 2 to Ex. 1 at 170, 173. In 2010, at the trough of the market, he omitted sales and leasing as a separate line item, noting only that it was part of his "All other Project Costs" figure. Ex. 1, Tab 12 at 703. Mr. Shorett, however, was able to back-calculate that figure to determine that it was $354,900, or 3.0% of the project value. See Ex. 13, line 13. These figures can be summarized as follows:

Year	2007	2008	2010
Page	Ex. 2 to Ex. 1 @ 202	Ex. 2 to Ex. 1 @ 170, 173	Ex. 13
Project Value	15,650,000	15,565,000	11,830,000
Sales & Mktg. Costs	384,750	933,900	354,900
Percent	2.46%	6.00%	3.00%

Such inconsistency does not instill confidence in the rigor or reliability of Mr. O'Connor's analyses.

Disappearing TDRs. In his analyses in 2007 and 2008, Mr. O'Connor included a value for transferrable development rights ("TDRs") of $340,000. See Ex. 2 to Ex. 1 at 181, 276-78. In the 2010 analysis prepared for the Examiner proceeding, he omitted that value altogether. Ex. 1, Tab 12 at 691. Despite having provided two pages of explanation for his approach to assessing the value of TDRs in 2007, he excused the lack of TDR value in 2010 simply by noting: "Not currently believed to be applicable." Ex. 1, Tab 12 at 691. Again, this is the very lack of detail that Mr. O'Connor was quick to label as a "red flag" when criticizing Mr. Shorett. In his testimony, Mr. O'Connor pointed to the current lack of demand for TDRs, but he conceded that the rights may be held until the market recovers. Mr. Shorett confirmed that the Eitel Building would qualify for TDRs, a point that was not rebutted. See Ex. 12. The TDR value should be included.

(4) Mr. O'Connor incorrectly ignored other potential sources of value to a renovation scenario, including the availability of low-income housing tax credits.

In addition to shifting certain assumptions and methodology in ways that undermine his credibility, Mr. O'Connor also consistently discounted other potential sources of value to a renovation scenario.

Value of the existing building permit. An approved set of plans already exists to renovate the Eitel Building. Ex. 2. Nevertheless, Mr. O'Connor included a standard, 5% escalation for architect and engineering costs. Ex. 1, Tab 12 at 697. In his testimony, Mr. O'Connor conceded that he could have given some credit for the value of the work already expended on the existing permit.

Value of the parking option. Mr. O'Connor assumed that no parking would be available for tenants of a renovated Eitel Building. He did not consider whether the rental values he used would be enhanced by the availability of parking next door as secured by an agreement between the Owner and the owner of the property to the north. See Ex. 5.

Value of low-income housing tax credits. Most significantly, Mr. O'Connor disregarded the potential value of low-income housing tax credits ("LIHTC"). The Owner's initial reason for ignoring that value proved to be incorrect, and the Owner's subsequent attempt to run from that value in rebuttal was unpersuasive.

Mr. O'Connor's reports do not discuss LIHTC. He either overlooked them as an option, or concluded that they would not be available as a legal matter. Consistent with the latter possibility, the Owner's attorney reported to the Board that LIHTC are not available in addition to historic preservation tax credits. Ex. 2 to Ex. 1, cover letter at 5. That was proven to be incorrect through Mr. Shorett's unrebutted testimony. See, e.g., Ex. 11. As a legal matter, LIHTC are available.

Mr. O'Connor was therefore likely caught off guard by Mr. Shorett's limited report. Using Mr. O'Connor's own methodology, Mr. Shorett demonstrated that a developer could pay the Owner roughly $1,400,000 for the Eitel Building (meaning an "after" value just below the $1,650,000 "before" value calculated by Mr. O'Connor), factor in a developer's profit of approximately 13% (of either value or costs), and still undertake a feasible residential development using LIHTC. See Exs. 10 and 13.

The Owner's experts' attempts to rebut Mr. Shorett's conclusion were unpersuasive. Mr. O'Connor incorrectly asserted that a LIHTC-based project could use no private equity. Mr. O'Connor ultimately admitted that there is no legal bar to the use of private equity, only that it would involve locking up equity for longer than what he believed a limited partner would be willing to do. Under his logic, the cash flow that would inure to the benefit of the limited partner means nothing; it can be a huge cash flow or a trickle, but either way the limited partner would never put up any private equity for the renovation. This is flat wrong, and Mr. O'Connor eventually conceded that any investment of private equity would involve weighing the cost of locking up the equity against the benefit of the tax credits and cash flow. He also conceded that he did no analysis to probe the reasonableness of that tradeoff; he simply assumed that the cash flow calculated by Mr. Shorett could not entice a limited partner to put up any private equity (even the modest amount assumed by Mr. Shorett). Mr. O'Connor also did not consider the

possibility of a low-income-housing provider, another non-profit organization, or the City contributing equity to make a low-income housing project more feasible. See, e.g., Ex. 36 (City Notice of Funding Availability).

The Owner's experts failed in their attempts to paint a LIHTC-based project as unlikely. Plymouth Housing Group ("PHG") offered the Owner $2.25M in 1999, see Ex. 6, and Mr. O'Connor testified that there has been no significant change in LIHTC law since then—if a LIHTC-based project made sense then, there is no reason to think that it would not make sense now. As if to prove that very point, Mr. Nimmer testified that PHG inquired about the Eitel Building's availability this year, after the Board's decision to recommend C&I. The record is rife with examples of low-income housing projects in downtown, many of them in older—even landmarked—structures in the center of downtown and not far from the Eitel Building. See, e.g., Exs. 11, 34, 37, and 38.

The Owner's experts' attacks against Mr. Shorett missed the mark. First, the purpose of Mr. Shorett's written report is clear and limited. Especially given that it was offered only in the context of a quasi-judicial proceeding where there was opportunity to cross-examine him and where the Owner put up two experts just to rebut him, there is no possibility that the Examiner was misled by the limited natured of Mr. Shorett's report.

Second, Mr. Shorett did not need to repeat the detail of Mr. O'Connor's report; he followed Mr. O'Connor's methodology using different assumptions about the availability of LIHTC, and he showed the relevant calculations using the same format and with the same degree of detail employed by Mr. O'Connor. Mr. O'Connor's critique of Mr. Shorett for lacking details is therefore unfounded in addition to being hypocritical—as documented above, Mr. O'Connor neglected to support several key calculations in his report.

Finally, Mr. Gibbons complained about using value figures from a more normalized market, saying it would be "charting new appraisal theory that goes where no person has gone before, as far as I'm concerned." Rec. 4/15 at 5:10. Even if that complaint were well founded, it undermines Mr. O'Connor's work much more than it does Mr. Shorett's. Mr. O'Connor dismissed the fact that his 2010 report used current values that were in the trough of the market by noting that neither of his prior reports demonstrated a feasible project.[12] But his 2008 report—generated at the height of the market—rejected use of current rental values as an "onus" and instead used "prospective" values. Ex. 2 to Ex. 1 at 155-56. Even if Mr. Gibbons is correct now and Mr. O'Connor was incorrect in 2008 (and we have no way of resolving that disagreement), then Mr. O'Connor's 2008 report and its deflated rental values should be ignored, as should his claim that, even in good times, no renovation made sense. As for Mr. Shorett's reliance on more "normalized" values, that affected his calculation of revenue coming only from retail and storage rents—or just 27% of the project's potential rent revenue. See Ex. 10.[13] The vast majority of the remaining revenue (from low-income residential rents) would be unaffected

[12] As noted above, that was incorrect for 2007, which would have shown a feasible apartment project had Mr. O'Connor employed the full "feasibility analysis/development approach" methodology.

[13] ((Potential retail rent, $134,480) + (Potential storage rent, $25,920)) / (Potential total rent, $594,560) = 0.27.

by market assumptions because it would be capped by law. Therefore, even if one were to believe Mr. Gibbons' current testimony about the use of prospective values and reject Mr. O'Connor's contrary representation in 2008, that would have only a limited impact on Mr. Shorett's calculations.

The technicalities raised by the Owner's counsel do nothing to undermine LIHTC as a potential source of value overlooked by the Owner. It does not matter that the Board's recommended C&I do not expressly list LIHTC as an incentive: LIHTC are not a City program (so its absence from the C&I document will not preclude use of LIHTC) and, if it really matters, the Examiner may modify the recommended C&I to mention the availability of LIHTC. SMC 25.12.560.B Noting how the Owner has overlooked LIHTC is not tantamount to a restriction on the use of the building. The fact that Mr. O'Connor did not analyze LIHTC, and then did so incorrectly only through rebuttal, is yet another indication that the Owner has not met its burden of proving that the imposition of the recommended C&I will deprive the Owner of a reasonable economic return—even on the incorrect assumption that the C&I will limit future alterations to within the shell of the existing building. Given the other reasons to doubt the reliability of Mr. O'Connor's conclusions, there is no basis for finding that the Owner has proven that other renovation scenarios would not be feasible.

2. The Owner has not attempted to meet, and could not sustain, its burden of proving no reasonable economic use.

The "reasonable economic use" standard in SMC 25.12.580, even if not defined, is necessarily different from the "reasonable economic return" standard in SMC 25.12.590. See Connor, LP-07-001, Findings and Decision at Conclusions 7 and 14. The Owner presented no expert testimony on whether the recommended C&I would deprive the Owner of a reasonable economic use, even assuming incorrectly that the recommended C&I would restrict future development to the existing shell of the Eitel Building. Cf. Ex. 1, Tab 12 at 603-06 (O'Connor report limited to the factors in SMC 25.12.590). The Owner has therefore failed to sustain its burden of proving a deprivation of reasonable economic use.

As discussed above, given the infirmities of Mr. O'Connor's analyses, the Owner has not proven that reasonable uses of the Eitel Building involving renovation would be unavailable. But even if the Owner were unable in today's climate to renovate the building (and even if the Owner had proven that no renovation would ever be possible—something the Owner did not attempt to do), continuing its current use would be reasonable. The Owner has made but one use of the Eitel Building for 35 years: as retail rental for the lower floors and an exterior surface for billboards, while doing the minimum necessary to ensure the structural stability of the upper floors. Even allowing the Owner to disregard the $80,000 Opus payment as income, but properly omitting legal and accounting fees as a building "operating" expense, the Owner has realized an average annual net income of $160,000 over the past eight years:

	2002	2003	2004	2005	2006	2007	2008	2009
Reported Net Operating Inc.	124,919	159,437	170,516	164,340	86,865	(19,722)	132,679	107,664
Add Reported Legal & Acctg.	4,341	2,774	509	450	56,901	145,079	77,162	67,420
Actual Net Operating Inc.	129,260	162,211	171,025	164,790	143,766	125,357	209,841	175,084

See Ex. 2 to Ex. 1 at 171; Ex. 1, Tab 12 at 708.

As discussed above, no evidence was offered to suggest why this use and general cash flow cannot continue for another 35 years. The Owner testified that he paid just $190,000 for this property in 1976. The Owner currently enjoys an average annual net cash flow equal to nearly 85% of that purchase price. The Owner professes no willingness to sell the property. Even if the Owner were limited to doing what the Owner has been doing for the past 35 years—and the Owner has not proven that to be the case—that would still have to be considered a reasonable economic use for the Owner.

BEFORE THE CITY COUNCIL

OF THE CITY OF SEATTLE

In the Matter of Controls & Incentives for

THE EITEL BUILDING
1501 Second Avenue

Hearing Examiner File:
LP-10-001

Landmark Preservation Board File:
22/10

1507 GROUP'S REPLY BRIEF ON APPEAL OF HEARING EXAMINER'S RECOMMENDATION

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I. REPLY INTRODUCTION

The Hearing Examiner committed reversible error when she failed to follow the procedures prescribed under the Seattle Municipal Code ("SMC") 25.12, Subchapter V, ignored the obligation to review the Board's recommendations for Controls & Incentives based on substantial evidence and applicable law, and improperly imported the procedures for certificates of approval. The Hearing Examiner committed further error by concluding that her review was *de novo* and allowing evidence that was not considered by the Board at the time it made its recommendation. Indeed, the Board has yet to offer any evidence ~ let alone the substantial evidence required ~ that supported its recommended controls. Review of the record also amply demonstrates that the Board did not following the Council's mandate under SMC 25.12.590 to analyze the exclusive factors for determining whether the controls imposed would deprive the Owner of a reasonable economic use of the Eitel Building. Because the controls imposed cannot be sustained, the Owner requests that the City Council reject the recommended controls and enact an ordinance pursuant to SMC 25.12.640.B(3) that imposes no controls on the Eitel Building.

The Board's central argument questions the relevance and purpose of negotiating the Controls & Incentives for any project. Indeed, if the Board's position is to be followed, why would it *ever* attempt to negotiate with an Owner on the Controls & Incentives? The Board would be better to simply ignore the Owner during these supposed negotiations and impose broad and vague controls, such as "alterations of the exterior of the structure will require a certificate of approval." This is exactly what has occurred, and this is exactly why the Owner appeals. The process used for the Eitel Building was not the process dictated by the ordinances enacted by this Council. It was not the process followed by other hearing examiners on Controls & Incentives recommendations. The process employed by the Board and the Hearing Examiner for the Eitel Building was fatally flawed, and the Owner is

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entitled to a remedy that only this Council can provide ~ to reject the recommended controls.

II. ARGUMENT

The Board spends more than half of its brief obfuscating the issues before the Council. The appeal before the Council is quite simple. Did the Hearing Examiner apply the right burdens and standards and, in doing so, or failing to do so, did she properly examine the reasonable return and reasonable economic use of the Eitel Building?

In the Owner's opening brief it argued that:

- The Hearing Examiner failed to apply the correct standard of review required by SMC 25.12.560(B);
- The Hearing Examiner relied on the wrong standards and based her decision upon the standards for a certificate of approval under SMC 25.12.750 (Conclusion No. 7, No. 8, No. 11; Applicable Law 33);
- The Hearing Examiner's Recommendations on proposed controls were unsupported under applicable law and/or substantial evidence in the record in violation of SMC 25.12.560 (Conclusion Nos. 6–12);
- The Hearing Examiner's Recommendations prevent the Owner from realizing a reasonable return on the Eitel Building in violation of SMC 25.12.570 and SMC 25.12.590;
- The Hearing Examiner's Recommendations also deprive the Owner of reasonable economic use of the Eitel Building in violation of SMC 25.12.580.

The Hearing Examiner's conclusions were in error and served only to compound the mistakes made by the Board and the Department of Neighborhoods' staff. The Board was supposed to engage in a collaborative process in negotiating the Controls & Incentives Agreement, but it did not. Rather, the Board largely disregarded the expert reports and documentation provided by the Owner and refused to consider the factors prescribed by SMC 25.12.590. In its belated epiphany, the Board now embraces the Hearing Examiner's conclusion that the Owner's evidence was based on a "false premise." This premise, however, was the only premise that the Board considered when it was supposed to be

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negotiating with the Owner: that is, whether the controls imposed would leave the Eitel Building without an economic use. As the Owner conclusively demonstrated and the Board failed to timely refute, the recommended controls will make the Eitel Building a liability from which the Owner cannot recover. Accordingly, the controls must be rejected by the City Council.

A. The Hearing Examiner's Conclusion Misapplied the Seattle Municipal Code

1. The Hearing Examiner Misunderstood The Burden Under SMC 25.12.560.

The Council must reject the misdirection of issues by the Board, which attempts to buttress the Hearing Examiner's conclusion with after-the-fact rationalization. Moreover, the Council should not be persuaded by the Board's twisted interpretation of the otherwise unambiguous mandate to the Hearing Examiner in SMC 25.12.560(B):

> The Board's recommendation on proposed Controls & Incentives must be supported by applicable law and substantial evidence in the record. The appellant bears the burden of proving that the Board's recommendation should be rejected or modified.

Under this provision, controls that are not based on applicable law or inconsistent with the evidence cannot be sustained. The Board must make its *prima facie* showing that its decision complies with the law and is supported by its evidence. To ignore this provision would render the first sentence of subparagraph B meaningless. *See Whatcom County Fire District v. Whatcom County,* 115 Wn. App. 601, 610, 215 P. 3d 956 (An ordinance is interpreted to give full affect to its plain meaning, which is "discerned from the ordinary meaning of the language at issue, the context of the statute in which that provision is found, related provisions, and the statutory scheme as a whole."). Once the *prima facie* showing is made, the burden shifts to the Owner to prove that the recommendation should either be rejected or modified. *See* SMC 25.12.560(B).

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For the Eitel Building, the Board's reasoning would mean that it could ignore the evidence provided by the Owner, make its decision on whatever basis it could conceive, and wait until after the Hearing Examiner's hearing before slipping in another development scenario as its *ex post facto* justification for the controls it chose to impose. To not require the Board to actually base its recommended Controls & Incentives on applicable law and substantial evidence **before it makes its recommendations** would render the plain meaning of SMC 25.12.560(B) as meaningless. Such a reading is inconsistent with the City Council's clear mandate and contradicts long-standing principles of statutory construction to give each provision its plain meaning.[1]

In rejecting this obligation, the Board argues that it "would have to hire outside experts to undertake a formal financial impact analysis before its meeting on recommended controls." Response Brief at 12, 20. In fact, that is precisely the Board's responsibility, as it has undertaken on other Controls & Incentive recommendations. In *The Bon Marche Stables* matter, LP-08-004 (Dec. 16, 2008), the Owner initially provided the Board with its appraisal report. The Department then retained an independent appraisal firm to review the Owner's expert's report. *Id.*, Findings of Fact 15 and 16. After an impasse was declared, the Hearing Examiner reviewed the competing appraisal documents and other expert testimony. *Id.*, Conclusions 4-15. In rejecting the Department's controls, the Hearing Examiner reviewed the exclusive factors provided by SMC 25.12.590 and concluded that the Board's evidence did not support the recommended controls. *Id.*, Conclusion 16.

Similarly, the Board acknowledged that it retained an expert when it recommended Controls & Incentives for the *Harry Whitney Treat House*, LP-06-001 (December 6, 2006).

---

[1] The Board's recommendation and the Hearing Examiner's conclusion reflect arbitrary and capricious reasoning in violation of the Owner's constitutional rights. *See Maranatha v. Pierce County*, 59 Wn. App 795, 804, 801 P.2d 985 (1990)(finding arbitrary and capricious conduct by local government when its decision is made "without consideration and in disregard of the facts"); *see also* 1507 Group's Appeal of Hearing Examiner's Recommendation, p. 15.

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The Department's expert provided it with input that resulted in the staff revising its controls. *Id.*, Finding of Fact No. 26. Ultimately, the hearing examiner evaluated the basis of the Department's recommended controls and its presentation of each of the factors under SMC 25.12.590 before she concluded that controls were supported by applicable law and substantial evidence. *See id.* Conclusion, ¶¶9 and 10 ("The factors that are to be considered in determining a reasonable return, are those listed in SMC 25.12.590.... Reviewing the record as a whole, the Board's evidence was credible and more persuasive as to current market value and returns."). Thus, the hearing examiner concluded that the Board made its *prima facie* showing, which the owner failed to rebut.

2. The Hearing Examiner Erred By Allowing Extraneous Evidence That Had Not Been Relied Upon By The Board When It Recommended Its Controls

The Hearing Examiner's hearing was not a "do over" as the Board would have the Council believe. The Board must justify its recommended Controls & Incentives with substantial evidence and applicable law. The Board cannot use the opportunity of a Hearing Examiner hearing to present never-before considered information as its after-the-fact justification of its prior recommendation. The Board's response incorrectly suggests that the Owner believed that the review should be "closed record." Owner argues no such thing. Rather, the Owner argues that the evidence presented should go to support the rationale articulated by the Board at the time the Controls & Incentives Agreement was recommended.

The Owner agrees that the Hearing Examiner hearing is open record. However, the Board confuses an open record predecision hearing with an open record appeal hearing:

> An open record hearing may be held prior to a local government's decision on a project permit to be known as an "open record predecision hearing." An open record hearing may be held on an appeal, to be known as an "open record appeal hearing," if no open record predecision hearing has been held on the project permit.

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RCW 36.70B.020(3) (emphasis added). An open record predecision hearing is one in which the decision making authority accepts public comments during the hearing and considers all testimony and evidence before rendering its decision. *See Humbert v. Walla Walla County*, 145 Wn. App. 185, 191, 185 P.3d 660 (2008). By contrast, the Eitel Building Controls & Incentives hearing was an appeal hearing. *See* HEARING EXAMINER RULES OF PRACTICE AND PROCEDURE §2.14 ("Although Hearing Examiner hearings are open to the public, those who are not parties are generally not permitted to testify in appeal hearings unless called as witnesses by a party.").

To be sure, SMC 25.12.560 directs the Hearing Examiner to assess whether the recommendation made by the Board on the proposed Controls & Incentives is "supported by applicable law and substantial evidence in the record." In other words, the Hearing Examiner was obliged to consider the evidence relied upon by the Board in making its recommendations.[2] The Hearing Examiner erred by allowing the evidence and testimony that was not used nor could have been relied upon by the Board when it developed its recommendation. The Board has acknowledged that it could not have relied on the evidence presented at the hearing when it made its recommended controls. The Board's experts all testified that they did not rely on the applicable law, SMC 25.12.590, when preparing their analysis. The Board's arguments offered in Appendix B of its Response Brief appeared for the first time after the Board made its recommendation and were based on considerations that were extraneous to the SMC's provisions. Accordingly, the error by the Hearing Examiner must be reversed by the Council.

[2] At the start of the hearing, the Owner filed Motion to Exclude Evidence presented by the Board, which included testimony, documents and reports not previously offered to the Owner or considered by the Department in making its decision. Further, the Owner sought to exclude witnesses offered by the Department but who in fact were representing the interest of a third-party that was not a party to the proceedings. In relying on her faulty presumption that the appeal was a predecision hearing, the Hearing Examiner allowed the evidence and witnesses.

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3. The Hearing Examiner's Recommended Controls Are Inconsistent With Past Decisions On Controls & Incentives

By importing the provisions of the Certificate of Approval process, the Hearing Examiner substantially deviated from the provisions of SMC 25.12.560-590. Hearing examiners have considered only two cases contesting Controls & Incentives in the last ten years, *The Bon Marche Stables* and *Harry Whitney Treat House* matters cited above. Noteworthy is the fact that neither of these cases makes reference to the Certificate of Approval process as the appropriate forum to consider development options for the designated landmark. Moreover, neither case found that the Hearing Examiner's review is made *de novo.*

Either the Board's argument does not make sense, or the ordinance does not make sense. To be clear, the code ALWAYS will require a Certificate of Approval when a control is imposed. *See* SMC 25.12.090. The very inclusion of the exclusive factors found in SMC 25.12.590 requires that the Board examine whether the controls, if approved, would leave the owner without a reasonable economic return on the building. By relying on the Certificate of Approval process for the Controls & Incentives Agreement, the Hearing Examiner conflated these two separate code provisions, rendering the latter as superfluous.

B. The Board And Department Ignored Their Directive Under The SMC To "Negotiate" The Controls & Incentives Agreement.

The Board and Department were under an obligation to negotiate with the Owner on a Controls & Incentives Agreement. SMC 25.12.490 ("The Board staff shall attempt to commence negotiations with the owner on the application of Controls & Incentives to the site, improvement, or object, regarding the specific features or characteristics identified in the Board's report on designation.") The Board ignored entirely this obligation, as demonstrated in the record by the lengthy letters from the Owner and the summary dismissal of the evidence by the Board and staff. *See* Exhibit 2 (showing vast amounts of

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information provided to the Department on its request, and then summary dismissals of the information as insufficient).

The Board makes much of the Hearing Examiner's conclusion that the Certificate of Approval process is "collaborative." Board's Response at p. 4. This supposed spirit of collaboration never materialized during the Controls & Incentives negotiations. Why should anyone expect such collaboration to be a given before the same players in the Certificate of Approval process?

The Board's starting point is improper: the existence of a "standard" agreement, in itself, suggests a lack of negotiation. The Owner repeatedly provided information and supporting details based on the ever-changing position by the Board and staff. *Id.* Yet when it came time to make a recommendation, the Board and staff asked questions that speak to the very core of this dispute. The official minutes from the Board meeting where the Controls & Incentives were adopted show that the Board was encouraged to merely adopt "standard" language with minimal alteration:

> She [Ms. Sodt] said the recommended Controls & Incentives for the building is based on a standard agreement, and the only unique aspect of the agreement is that staff recommends including language stating that the Certificate of Approval process would not preclude the owner from infilling the light well on the west elevation, although the details of the infill would need to be reviewed by the Board.

Ex. 33, p.8. Inherent in this approach with the Board of volunteers is an improper presumption that at this stage it is up to the Owner to convince the Board as to what controls should be applied.

C. The Board Now Seeks To Change the Basis of Its Recommendation on Controls.

The Board now claims that all of the information provided to the Board and its staff from the Owner was based on a "false premise." It was not false, however. It was the exact same premise provided to the Owner by the Board and staff. The "premise," of course, is

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whether preservation of the Eitel Building will provide the Owner with an "economic return." The Board now attempts to recast that premise as something else—a possible development scenario that the Board had not previously considered.

Indeed, in the three years in which the Owner was attempting to negotiate with the Board and staff, and through more than three days of hearing in front of the Hearing Examiner, this premise remained the same. The Department never suggested that the premise was false or another premise should be considered. When the full Board considered the controls to be imposed on the Eitel Building, it never suggested that the Owner should analyze a different development scenario or based its evaluation on another premise. The Council is invited to review the 19 pages of minutes in which Board could only offer other incentives as a means for the Owner to achieve an economic return and express vague doubts as to the Owner's expert reports.[3] *See* Exhibit 33.

The Board states that it was "both overwhelmed and unconvinced by the series of dense appraiser and other expert reports and technical documents produced by the Owner." Response at 11. Yet, SMC 25.12.490 and 500 impose on the Board the commitment of undertaking a meaningful review when negotiating with the Owner on the Controls & Incentives Agreement. Undeniably, the Board never seriously entered into negotiations with the Owner as required by the SMC. The Owner continued in vain to negotiate and respond to statements offered by Department staff and later by the Board. Both staff and the Board saw fit to make comments on material that they now claim they could not understand or could not be bothered to take the time to actually review.

[3] The Board's Response Brief asks the Council to "look skeptically on the one-sided citations in the opening brief to the Owner's experts' reports." Response Brief at 13. The Owner requests that the Council consider the fact that the Board never produced any reports until the Hearing Examiner's hearing.

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III. CONCLUSION

SMC 25.12.560(B) is unambiguous: "The Board's recommendation on proposed Controls & Incentives must be supported by applicable law and substantial evidence in the record." If this provision is to have any meaning, it must be applied faithfully by the Board and the Department. If the procedures prescribed by the SMC for determining the controls to be imposed on an historic building are to serve any purpose, they must be applied independently and not morphed into the procedures for a Certificate of Approval. To ignore these basic statutory mandates would allow the Board to disregard its obligations and concoct any "premise" or other development scenario after it makes its recommendation. Owners would be left to second guess what future scenarios could be raised by the Board at a contested hearing. This would provide owners without any predictability in what process should be followed and create insurmountable obstacles, which are precisely the consequences that the code is intended to avoid.

The Owner of the Eitel Building did exactly what it was supposed to do in accordance with the SMC and the hearing examiners' conclusions on other Controls & Incentives recommendations for determining the economic consequences to an Owner of an historic structure. The Hearing Examiner impermissibly changed the rules by: misapplying the SMC requirement that the Board's recommendation be based on substantial evidence and applicable law; treating the hearing as a *de novo* review; conflating the procedures for Controls & Incentives with Certificates of Approval; and allowing the Board to rely on evidence that had not been used in preparing its recommended controls.

The City Council is empowered to reject the conclusions of the Hearing Examiner and the Controls recommended by the Board. Due to the mishandling of this process by the Hearing Examiner, the expense spent by the Owner as the Board refused to develop any support for its desire to implement the "standard" controls, and the clear evidence showing

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the financial ruin that will be caused if the controls are imposed, the Council must reject the controls.

Dated this 1st day of December, 2010.

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By: _____
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CERTIFICATE OF SERVICE

I hereby certify that on the 1st day of December, 2010, I caused to be served the foregoing *1507 Group's Reply Brief on Appeal of Hearing Examiner's Recommendation* on the following parties at the following addresses:

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600 Fourth Avenue, 4th Floor
Seattle, WA 98104

by:

- ☐ U.S. Postal Service, ordinary first class mail
- ☐ U.S. Postal Service, certified or registered mail, return receipt requested
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- ☐ facsimile
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BEFORE THE CITY COUNCIL

OF THE CITY OF SEATTLE

In the Matter of Controls and Incentives for **THE EITEL BUILDING** **1501 Second Avenue**	Hearing Examiner File: **LP-10-001** Landmark Preservation Board File: **22/10** **NOTICE OF APPEAL OF HEARING EXAMINER'S FINDINGS AND RECOMMENDATIONS**

PLEASE TAKE NOTICE, property owner 1507 Group, LLC (the "Owner") hereby appeals the Hearing Examiner's Findings and Recommendation dated June 9, 2010 in the above referenced matter and attached hereto as **Exhibit A**.

I. STATEMENT OF OBJECTIONS

The Owner objects to the Hearing Examiner's Conclusions of Law, Findings and Recommendation to impose controls and incentives on the following grounds:

1. The Hearing Examiner's Findings and Recommendations applied the incorrect law by relying on the factors relevant to certificates of approval under SMC 25.12.750. A certificate of approval for the Eitel Building was not before the Hearing Examiner in this proceeding.

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ORIGINAL

2. The Hearing Examiner's Findings and Recommendations failed to apply the correct standard of review required under SMC 25.12.560.B.

3. The Hearing Examiner relied on unsupported assertions and unsubstantiated conclusions from the coordinator for the Landmark Preservation Board concerning certificates of approval allowing additional height.

4. The Hearing Examiner's recommendation on proposed controls and incentives is not supported by applicable law and/or substantial evidence in the record and therefore is in violation of SMC 25.12.560.

5. The Hearing Examiner's recommendation on proposed controls prevents the Owner from realizing a reasonable return on the site located at 1501 Second Avenue in violation of SMC 25.12.570 and SMC 25.12.590.

6. The Hearing Examiner's recommendation on proposed controls erroneously considers factors other than and in addition to the exclusive factors listed under the Landmark Preservation Ordinance for determining a "reasonable return" on the site at 1501 Second Avenue and is therefore in violation of SMC 25.12.590.

7. The economic standard specifically applicable to controls and incentives is SMC 25.12.570 requiring "reasonable return." In addition, the Hearing Examiner's recommended controls and incentives deprive the Owner of reasonable economic use of the site at 1501 Second Avenue in violation of SMC 25.12.580.

8. Owner reserves the right to supplement and/or offer additional objections and supporting memoranda pursuant to the procedures established by the City Council under SMC 25.12.630.B.

II. RELIEF REQUESTED

Owner respectfully requests that the City Council reject the Controls and Incentives recommended by the Hearing Examiner and enact an ordinance that imposes no controls and incentives on the Eitel Building located at 1501 Second Avenue, because imposition of

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controls would prevent Owner from realizing a reasonable return on the site in violation of SMC 25.12.570.

Alternatively, the Owner requests the City Council modify the Hearing Examiner's recommended controls to expressly allow alterations to the exterior of the Eitel Building for increased height to the limit allowed by law and without setback from the existing building perimeter.

III. CONTACT INFORMATION OF THE OWNER

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Dated this 23rd day of June, 2010.

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CERTIFICATE OF SERVICE

I hereby certify that on the 23rd day of June, 2010, I caused to be served the foregoing *Notice of Appeal of Hearing Examiner's Findings and Recommendations* on the following parties at the following addresses:

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Karen Gordon
Department of Neighborhoods
City of Seattle
700 Fifth Avenue, Suite 1700
Seattle, WA 98124-4649

by:

- ☐ U.S. Postal Service, ordinary first class mail
- ☐ U.S. Postal Service, certified or registered mail, return receipt requested
- ☒ hand delivery
- ☐ facsimile
- ☐ electronic service
- ☐ other (specify) _____

James C. Anderson
Secretary to Lawrence A. Costich

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Exhibit A

Exhibit A

FINDINGS AND RECOMMENDATION
OF THE HEARING EXAMINER FOR THE CITY OF SEATTLE

In the Matter of Controls and Incentives for

THE EITEL BUILDING
1501 Second Avenue

Hearing Examiner File:
LP-10-001

Board File:
22/10

Introduction

The Landmarks Preservation Board issued a recommendation on controls and incentives for the Eitel Building, located at 1501 Second Avenue, and the property owner timely filed an objection to the recommendation. The matter was heard before the Hearing Examiner on April 13, 14, and 15, and May 12, 2010. Parties represented at the hearing were the property owner, 1507 Group LLC (Owner), by Lawrence A. Costich and Curtis R. Smelser, attorneys-at-law; and the Landmarks Preservation Board (Board), by Roger D. Wynne, Assistant City Attorney. The Examiner visited the property, and the record was held open through May 28, 2010 for post-hearing filings.

For purposes of this recommendation, all section numbers refer to the Seattle Municipal Code, as amended, (SMC or Code) unless otherwise indicated. Having considered the evidence in the record and inspected the site, the Examiner enters the following findings of fact, conclusions and recommendation on controls and incentives.

Findings of Fact

1. The subject property is known as the Eitel Building (building) and is addressed as 1501 Second Avenue. It is located on the northwest corner of the intersection of Second Avenue and Pike Street, within the central business district and two blocks east of the Pike Place Market. It abuts the 38-story Opus condominium tower on the north and is bordered on the west by an alley that runs parallel to Second Avenue. Across the alley is the two-story Liberty Building.

2. The building is a seven-story rectangular structure with tan-colored brick cladding and terra-cotta ornamentation. Six stories were built in 1904 of unreinforced masonry with a steel column and lintel base support system on the southern and eastern sides, and an interior steel column and girder system supporting wood floor and roof framing. The seventh story was added in 1906. The southern and eastern façades are considered primary. Exhibit 26.

3. The building covers most of the 5,592-square-foot site and is approximately 90 feet tall. The basement extends partially under the adjoining sidewalk, and there is a light well that begins with the second floor on the western elevation.

4. The Owner purchased the building in 1975 as an investment in the hope that future renovation would be possible. When renovation to building code standards proved too costly, the Owner rented out the ground floor to commercial tenants and has kept the upper six floors vacant. The Owner also leases out billboard space on the west exterior of the building. Over the years, deterioration and earthquake damage have required structural work to stabilize the building.

5. Until recently, the zoning on the property was DMC (Downtown Mixed Commercial) 240, which would have allowed construction of a 240-foot building. However, in 2004, the Owner obtained a permit to renovate the building within the existing shell. Although the renovations proved too costly for the Owner to proceed, the building permit has been repeatedly renewed and remains active.

6. In 2006, the Owner learned that the property would be rezoned to its present zoning, DMC 240/290-400. The Owner determined that the new zoning would allow one property on the block to be developed to a height of 400 feet but would limit other development on the same block to a maximum height of 160 feet. The Opus tower to the north was to be constructed to approximately 400 feet. Therefore, the Owner decided to construct a 240-foot building on the subject property before the new zoning took effect.

7. The Owner hired an architect, who developed plans for a 22-story building with 92 residential units above 23,000 square feet of administrative office space and 3000 square feet of retail space. The proposal, which included demolition of the existing building, was reviewed in a meeting with the Design Review Board in February of 2006. Exhibit 18.

8. In August of 2006, the Landmarks Preservation Board (Board) designated the building as a landmark following nomination by Historic Seattle. The Board determined that the building "embodies the distinctive visible characteristics of an architectural style, period, or of a method of construction." *See* "Staff's Recommendation on Controls and Incentives" (January 13, 2010) attached to January 26, 2010 letter from Karen Gordon to the Hearing Examiner (Staff's Recommendation). The Owner then retained counsel to negotiate with the Board on a Controls and Incentives Agreement for the building.

9. Following designation, the Owner revised the development proposal for the site to remove the seventh floor and add a 16-story tower above the existing six-story building, preserving the south and east façades. The building would be 16 floors of residential above one level of retail use and five floors of office use. *See* Exhibit 29. The Design Review Board met to consider the revised proposal in October of 2006. Exhibit 19.

10. In January of 2007, the Owner filed a Master Use Permit (MUP) application, thereby vesting to the then-existing 240-foot zoning. At the same time, the Owner submitted the MUP drawings and a project description to the Board's staff and asked to schedule a meeting with the Board's Architectural Review Committee (ARC). Exhibit 27.

11. The ARC is a subcommittee of the Board composed of members with architectural expertise. The ARC is available to meet with an owner to review a proposal, and provide feedback and suggestions on it, before the owner seeks a Certificate of approval from the full Board. The process is collaborative, and the goal is to achieve a design solution that meets both the owner's needs and the Board's goal of preserving the designated historic features. Testimony of Sarah Sodt, 4/15/10 at 1:22. *See* SMC 25.12.750 (reproduced below).

12. A certificate of approval is required from the Board before the owner of a designated landmark may alter or significantly change the designated features or characteristics of the landmark. *See* SMC 25.12.080, .670.

13. The Board's coordinator testified that the Board has granted certificates of approval that resulted in the destruction of some designated features of landmark buildings when the aspects of the buildings that remained were sufficient to convey their historical importance. The coordinator cited two recent examples: the Pacific McKay Ford Building on Westlake Avenue, where the primary façades were removed and are in storage for future installation on a new development; and the Terminal Sales Annex Building at 1931 Second Avenue, a narrow building for which the Board approved retention of the street-facing façade and the addition of a multi-story tower atop the landmark. Testimony of Sarah Sodt, 4/15/10 at 1:22-1:26 and 2:20. She did not know of any certificate of approval application for construction of additional stories atop a landmark that has been denied. Testimony of Sarah Sodt, 4/15/10 at 2:22.

14. It is not necessary for controls and incentives for a building to be in place before an owner seeks a certificate of approval for proposed changes to it. Testimony of Sarah Sodt, 4/15/10 at 1:18.

15. Working with an architect not known to have experience with historical structures, the Owner presented the MUP proposal to the ARC in March of 2007. The ARC suggested that the architect consider an alternative that reduced the tower height and explore a tower setback. The ARC did not state that the design needed to stay within the existing shell of the building. Testimony of Sarah Sodt, 4/15/10 at 1:28-130.

16. To determine the economic impact that might result from controls and incentives that could be adopted for the building, the Owner retained an appraiser to evaluate the feasibility of three development scenarios. The first appraisal was produced on June 8, 2007. The three development scenarios evaluated were office and retail, residential condominium and retail, and residential apartment and retail. They were based on the renovation plans developed for the 2004 building permit. Thus, for each scenario, the appraiser assumed that forthcoming controls and incentives for the building would limit construction to the building's existing shell. *See* Tab 2 to Exhibit 1[1] at 211, 279, 289 and

[1] Tab 2 to Exhibit 1 consists of bound documents, the content of which is essentially the same as the compact disc included under Tab 2 of Exhibit 1. The page numbers referenced in Exhibit 1 and Tab 2 to Exhibit 1 are the Bates-stamped numbers at the bottom of the pages.

299. The appraiser concluded that none of the three development scenarios would be "expected to produce a sufficient return on investment necessary to attract capital to the project." Tab 2 to Exhibit 1 at 193.

17. Under the caption, "Extraordinary Assumptions and Limiting Conditions," the 2007 appraisal notes that the three development scenarios considered "are believed to reflect reasonable and realistic use constraints" that may be imposed on the property through the controls and incentives process. The appraiser reserves the right to modify the appraisal's conclusions if "any or all of the ... assumptions utilized prove to be in error." Tab 2 to Exhibit 1 at 211.

18. The Owner chose not to return to the ARC with a revised design proposal and, instead, filed an application for a certificate of approval in October for essentially the same proposal the ARC had reviewed in March. Exhibits 28 and 29. On November 5, 2007, the Board's staff sent the Owner an application checklist showing which pieces of the certificate of approval application were still missing.

19. On November 15, 2007, as part of the MUP process, the Director of the Department of Planning and Development (DPD) issued a SEPA determination of significance, requiring that an environmental impact statement be prepared to analyze the proposal's historic preservation and land use impacts. Exhibit 22. The Owner retained an environmental consultant to begin work on the EIS. Testimony of Richard Nimmer, 4/13/10 at 10:33.

20. On May 7, 2008, the Owner's appraiser issued an updated appraisal to evaluate the likely economic impact of controls that might be imposed on the building. Tab 2 to Exhibit 1 at 144. Again, the appraisal assumed that any of the three development scenarios would involve "essentially 'rebuilding' the existing seven-story improvement and, in addition, foregoing the opportunity to develop the site to the full extent of the remaining 15 stories." Tab 2 to Exhibit 1 at 172. Under these assumptions, the appraiser again concluded that none of the three scenarios would be capable of producing a sufficient return on investment to attract capital. Tab 2 to Exhibit 1 at 172.

21. The 2008 appraisal also considered the feasibility of the 22-story revised MUP proposal, including demolition of the building, for residential condominium use and residential apartment use. Assuming a minimum rate of return required to attract capital of 75 percent, the appraisal concluded that both of these development scenarios would be feasible. *See* Tab 2 to Exhibit 1 at 169, and 174-76.

22. The Owner believes that as a result of the landmark designation, the building is capped at 90 feet with the exception of a possible small "penthouse" addition. Testimony of Richard Nimmer, 4/13/10 at 10:30. However, the Owner acknowledged that if controls on the building did not prevent an increase in building height, the air rights above the building would be valuable to the owners of adjacent buildings. As an alternative to a tower atop the existing building, the Owner agreed that the air rights could be sold to help fund renovation of the existing building. Testimony of Richard

Nimmer, 4/13/10 at 11:18. The Owner's appraiser agreed that a purchase of air rights could make building renovation possible. Testimony of Brian O'Connor, 4/14/10 at 11:54.

23. On May 9, 2008, the Owner submitted the 2007 and 2008 appraisals to the Board, together with a letter from the Owner's architect, indicating that the application now included demolition of the building, and other materials required to complete the October 2007 certificate of approval application. Exhibit 31.

24. On April 22, 2009, the Owner inquired of DPD concerning the ramifications of placing the revised MUP application on hold while continuing to pursue a certificate of approval from the Board. DPD responded on May 8, 2009, that the Owner would need to terminate the certificate of approval process in order to remove the MUP from active status. Exhibit 24.

25. On May 14, 2009, the Owner notified the Board that it was withdrawing its application for a certificate of approval to demolish the building. Exhibit 25.

26. The Owner and Board continued to discuss controls and incentives for the building. On January 12, 2010, the Owner declared that the negotiations were at an impasse.

27. On January 20, 2010, the Board adopted recommended controls and incentives, which were forwarded to the Hearing Examiner on January 26, 2010. The recommended controls and incentives require that the Owner obtain a certificate of approval from the Board before making alterations or significant changes to the exterior of the building with the exception of the light well on the western elevation. *See* Staff's Recommendation.

28. The Owner timely filed a statement of objections to the Board's recommended controls and incentives. The objections state that the recommended controls are not supported by applicable law and substantial evidence in the record; prevent the owner from realizing a reasonable return on the site; resulted from consideration of factors other than, and in addition to the factors listed in SMC 25.12.590 for determining a reasonable return on the site; deprive the owner of a reasonable economic use of the site; and deny the Owner substantive due process and amount to an inverse condemnation (taking) of the site, in violation of the constitution.

29. In preparation for the hearing on the Owner's objections to the Board's recommended controls and incentives, the Owner's appraiser issued a March 30, 2010 summary appraisal of the property that updated information on its market value. Exhibit 1, Tab 11 at 489. The appraiser determined that the "highest and best use" of the property was to "hold for future development" and valued it at $2,500,000 under the "vested MUP" proposal, and $1,650,000 under the existing 160-foot zoning assuming that no controls were imposed. Exhibit 1, Tab 11 at 493, 582 and 587.

30. On April 7, 2010, the Owner's appraiser issued an updated appraisal to evaluate the economic impact of the imposition of controls on the property. Exhibit 1, Tab 12 at 603.

The appraiser again assumed that the Owner would be required to preserve the existing shell of the building other than the light well. Exhibit 1, Tab 12 at 626. And the appraiser again reserved the right to modify the conclusions in the report should the assumption on controls be proven incorrect. Exhibit 1, Tab 12 at 626. As in the earlier appraisals, the appraiser concluded that "rehabilitation of the existing improvements is not considered to be feasible" under the assumed controls. Exhibit 1, Tab 12 at 605.

Applicable Law

31. SMC 25.12.570 provides that "[o] n the basis of all the evidence presented at hearing," the Examiner is to determine whether to recommend that the proposed controls and incentives recommended by the Board be accepted, rejected or modified. Further, the Examiner "shall not recommend any control which is inconsistent with any provision of this chapter, or which requires that the ... [landmark] be devoted to a particular use," or that imposes any use restriction, control or incentive if the effect, alone or in combination, "would be to prevent the owner from realizing a reasonable return on the [landmark]." SMC 25.12.590 lists the factors to be considered in determining a reasonable return on the landmark.

32. SMC 25.12.580 states that "in no event shall ... any proceedings under or application of this chapter deprive any owner of a ... [landmark] of a reasonable economic use of such ... [landmark]."

33. SMC 25.12.750 lists the factors that the Board and Examiner are to take into account in considering an application for a certificate of approval. The factors relevant to this case are the following:

> A. The extent to which the proposed alteration or significant change would adversely affect the specific ... [landmarked] features or characteristics...;
>
> B. The reasonableness or lack thereof of the proposed alteration or significant change in light of other alternatives available to achieve the objectives of the owner and the applicant;
>
> C. The extent to which the proposed alteration or significant change may be necessary to meet the requirements of any other state law, statute, regulation, code or ordinance; [and]
>
> D. Where the Hearing Examiner has made a decision on controls and economic incentives, the extent to which the proposed alteration or significant change is necessary or appropriate to achieving for the owner or applicant a reasonable return on the ... [landmark], taking into consideration the factors specified in Sections 25.12.570 through 25.12.600 and the economic consequences of denial; provided that, in considering the factors specified in Section 25.12.590 for purpose of this subsection, reference to the times before or after the imposition of controls

shall be deemed to apply to times before or after the grant or denial of a certificate of approval;

....

Conclusions

1. The Hearing Examiner has jurisdiction over this matter pursuant to SMC 25.12.540.

2. The Owner's constitutional issues of inverse condemnation and substantive due process are beyond the jurisdiction of a quasi-judicial body, and the Examiner has not considered them. *See Yakima Cy. Clean Air Authority v. Glascam Builders, Inc.*, 85 Wn.2d 255, 257, 534 P.2d 33 (1975).

3. Under the scheme of Subchapter V. of Chapter 25.12 SMC, the Hearing Examiner's recommendation on controls and incentives is essentially *de novo*. The issue before the Examiner under SMC 25.12.560.B is whether the Board's recommended controls and incentives are supported by substantial evidence in the record before the Examiner. "Under the substantial evidence standard, there must be a sufficient quantum of evidence in the record to persuade a reasonable person that the declared premise is true." *Wenatchee Sportsmen Ass'n v. Chelan Cy.*141 Wn.2d 169, 176, 4 P.3d 123 (2000) (citations omitted). The "appellant bears the burden of proving that the Board's recommendation should be rejected or modified." SMC 25.12.560.B. The "appellant" in this case is the Owner.

4. The Owner objects to the Board's recommendation as not being supported by applicable law and substantial evidence in the record before the Board. As noted, however, the Examiner's review under the Code is *de novo*. Therefore, the record before the Board is immaterial in this proceeding.

5. The Owner asserts that the Board erroneously considered factors other than, and in addition to the exclusive factors listed in SMC 25.12.590 for determining a reasonable return on the site. However, the Owner did not establish what factors the Board considered in reaching its recommendation on controls and incentives. Moreover, the issue before the Examiner is not what the Board considered but whether the Board's recommended controls and incentives are supported by substantial evidence in the record before the Examiner.

6. The Owner's entire case, including all the work of the Owner's appraiser, rests on the premise that the Board's recommended controls would limit any development of the property to the shell of the existing building. Yet there is no evidence in record to support that premise.

7. The recommended controls require only that the Owner obtain a certificate of approval from the Board before making exterior alterations to the building, with the exception of eliminating the light well. Both the evidence in the record and the

applicable law demonstrate that the certificate of approval process is a collaborative one, designed to achieve both the owner's and City's needs with respect to the landmark.

8. The Owner argues that the addition of floors to the building would "significantly change and adversely affect" the features or characteristics specified in the designation, and that it is not clear the Board would approve such a change. However, the certificate of approval process exists to examine and, if possible, resolve such challenges. The ARC works with the owner toward development of alternative designs. The Board considers several factors, including the reasonableness of the proposed alteration in light of the alternatives available to achieve the owner's objectives. *See* SMC 25.12.750.B (Finding 33). The Code does not dictate a particular outcome, nor does it require preservation of all designated historic features. Moreover, past Board practice, including this Owner's experience with the ARC, demonstrates that approval of a tower above the landmark is in no way foreclosed.

9. The Owner states that if the Board had believed additional height was acceptable, it would have said so in its recommendation, as it did with the exception allowing infill of the light well. The Board is not a legislative body, and it is not clear that the rules of statutory construction apply to its recommendation. In any event, the fact that the Board did not include an exception for additional height above the landmark does not indicate that additional height is precluded; rather, it suggests that the addition of floors above the landmark would require the exploration of alternatives that is an inherent part of the certificate of approval process.

10. The Owner correctly asserts that the evidence fails to demonstrate that adding floors to the building could be accomplished and would provide the Owner a reasonable rate of return. The evidence does show that from 2006 through 2007, the Owner pursued the original 22-story MUP proposal that included preservation of the south and east façades and construction of a tower above the existing landmark. Working with an architect not known to have experience with historical structures, the Owner met with the Design Review Board and the ARC on the MUP proposal. Both bodies asked for revised alternatives, although for slightly different reasons. The evidence shows that in 2008, the Owner received an appraisal that indicated demolition of the landmark and sale of the property for construction of a 240-foot or 160-foot tower would result in a rate of return necessary to attract capital to the project. The evidence also shows that in 2008, the Owner decided to demolish the building and terminated the certificate of approval process. During the intervening two years, the Owner has directed resources toward convincing the Board that any controls and incentives placed on the landmark would prevent the Owner from realizing a reasonable return and deprive the Owner of a reasonable economic use. As a result, we do not know with certainty whether a tower can be built atop the landmark, and there is no evidence in the record on whether development available to the Owner through the MUP and certificate of approval processes would provide the Owner with a reasonable return and a reasonable economic use. The Board's recommended controls and incentives would afford the opportunity for development of the information necessary to make those determinations. *See* SMC 25.12.750.D (Finding 33).

11. The Owner drew an analogy between this case and In re Bon Marche Stables, LP-08-004, which also involved an owner's challenge to the imposition of controls and incentives that required a certificate of approval for exterior alterations. In that case, however, the Board did not dispute that the imposition of controls and incentives would limit future development to the shell of the existing building.

12. Because all of the Owner's evidence is based on an invalid assumption, the Owner has not met the burden of proving that the Board's recommended controls and incentives should be rejected or modified.

Recommendation

The Hearing Examiner recommends that the City Council accept the Board's recommendation on controls and incentives for the Eitel Building.

Entered this 9th day of June, 2010.

Sue A. Tanner
Hearing Examiner

Concerning Further Review

NOTE: It is the responsibility of the person seeking further review of a Hearing Examiner recommendation to consult appropriate Code sections to determine applicable rights and responsibilities.

SMC 25.12.620 provides as follows:

> Any party of record before the Hearing Examiner may appeal the recommendations of the Hearing Examiner regarding controls and incentives to the Council by filing with the City Clerk and serving on all other parties of record a written notice of appeal within fourteen (14) days after the Hearing Examiner's decision is served on the party appealing.

BEFORE THE CITY COUNCIL

OF THE CITY OF SEATTLE

In the Matter of Controls and Incentives for **THE EITEL BUILDING** **1501 Second Avenue**	Hearing Examiner File: **LP-10-001** Landmark Preservation Board File: **22/10** **STIPULATION PURSUANT TO SMC 25.12.850 TO EXTEND 90-DAY TIME LIMIT FOR CITY COUNCIL ACTION**

Property owner and Appellant 1507 Group, LLC and Respondent City of Seattle Department of Neighborhoods (collectively, the "Parties") by and through their respective attorneys, hereby stipulate and agree pursuant SMC 25.12.850.D to waive the time limits under SMC 25.12.640.A for City Council review and consideration of the above-captioned appeal. The Parties further stipulate and agree that the deadline for City Council action should not be extended beyond February 28, 2011.

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Dated this 30th day of July, 2010.

PETER S. HOMES
SEATTLE CITY ATTORNEY

By: Roger D. Wynne

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By authorization:

By: Roger D. Wynne for

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CERTIFICATE OF SERVICE

I certify that, on this date, I sent a copy of this document by email attachment, and caused a copy to be sent by First Class mail,:

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lcostich@schwabe.com
Attorney for Owners 1507 Group, LLC

the foregoing being the last known addresses of the above-named parties.

DATED this 30th day of July, 2010, at Seattle, Washington.

Roger Wynne

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City of Seattle
Legislative Department

Date: November 9, 2010

To: To Whom It May Concern

From: Ketil Freeman, Legislative Analyst, Council Central Staff

Subject: Appeal of 1507 Group, L.L.C. from a recommendation by the Hearing Examiner on landmark controls and incentives for the Eitel Building, 1501 Second Avenue (Quasi-judicial).

NOTICE IS GIVEN that the Council has received an appeal of the Hearing Examiner's recommendation on landmark controls and incentives for the Eitel Building, 1501 Second Avenue; and **NOTICE IS GIVEN**, that on December 8, 2010 at 9:30 a.m., the Council's Committee on the Built Environment (Committee) will take up the appeal. The appeal is a quasi-judicial action of the City Council and is subject to the Council's Quasi-judicial Rules. The Council's Quasi-judicial Rules were adopted by Resolution 31001 and are available at http://www.seattle.gov/council/legdb.htm.

- **Oral Argument.** The Committee, at its discretion, may, upon request, hear oral argument from those persons who submitted an appeal, those persons who submitted a response to the appeal, and any persons who have been permitted to intervene. If oral argument is permitted, each party of record will generally be permitted five minutes for oral argument, unless there are extraordinary circumstances, in which case the Committee shall determine the amount of time to allow. The parties-of-record who filed an appeal would go first and may reserve a portion of time for rebuttal. The Committee may ask questions or extend the time for argument at the discretion of the Committee chair. If permitted, oral argument on the merits of the proposal must be based on the evidence admitted into the record.
- **Instructions for Responding to the Appeal.** Parties-of-record may file a response to the appeal with the City Clerk no later than five p.m. on November 22, 2010. Replies to any response may be filed no later five p.m. on December 1, 2010. Responses and replies must be in writing and filed, along with a certification of mailing, with the City Clerk. Copies must also be mailed to those parties listed on the reverse of this memorandum. A certificate of mailing is a signed sworn statement that a document has been mailed by first class mail on the date stated in the certificate and to the persons named at the addresses listed in the certificate. The City Clerk is located at:

City Clerk
City Hall, Floor 3
City of Seattle
PO Box 94728
Seattle, WA 98124-4728

Questions concerning the meeting or the Council's Quasi-judicial Rules may be directed to Ketil Freeman by calling (206) 684-8178 or via e-mail at ketil.freeman@seattle.gov.

Print and communications access for Council meetings is provided on prior request. Please contact LaTonya Brown at (206) 684-5329 as soon as possible to request accommodations for a disability.

Attachments:
Appeal by 1507 Group, LLC, June 23, 2010
Opening Brief by 1507 Group, LLC, November 8, 2010

LAWRENCE A. COSTICH SCHWABE, WILLIAMSON & WYATT, P.C. US BANK CENTRE 1420 FIFTH AVENUE, SUITE 3400 SEATTLE, WA 98101	ROGER WYNNE ASSISTANT CITY ATTORNEY SEATTLE CITY ATTORNEY'S OFFICE 600 4TH AVENUE, 4TH FLOOR SEATTLE, WA 98104
CURT SMELSER SCHWABE, WILLIAMSON & WYATT, P.C. US BANK CENTRE 1420 FIFTH AVENUE, SUITE 3400 SEATTLE, WA 98101	KAREN GORDON DEPARTMENT OF NEIGHBORHOODS CITY OF SEATTLE 700 5TH AVENUE, SUITE 1700 SEATTLE, WA 98124

CERTIFICATE OF MAILING

I certify under penalty of perjury under the laws of the State of Washington that on November 9, 2010, I sent the following documents: *Notice of Appeal Hearing* for the Controls and Incentives Appeal by 1507 Group L.L.C., for the Eitel Building, 1501 Second Avenue, to the following listed persons by first class mail, postage prepaid, at the addresses listed below, those addresses being the last known post office address or interoffice mail stop of each.

LAWRENCE A. COSTICH
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CURT SMELSER
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ROGER WYNNE
LAW DEPARTMENT
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SARAH SODT
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SMT -17-00

KAREN GORDON
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ELAINE KO, CITY COUNCIL
CH-02-10

MICHAEL JENKINS, LEG
CH-02-10

KETIL FREEMAN, LEG
CH-02-10

Signed this 9th day of November at Seattle, Washington.

K F
(Signature)

Ketil Freeman
(Printed Name)

City of Seattle
Legislative Department

Date: January 3, 2011

To: To Whom It May Concern

From: Ketil Freeman, Legislative Analyst, Council Central Staff

Subject: Appeal of 1507 Group, L.L.C. from a recommendation by the Hearing Examiner on landmark controls and incentives for the Eitel Building, 1501 Second Avenue.

NOTICE IS GIVEN, that on January 12, 2011 at 9:30 a.m., the Council's Committee on the Built Environment (Committee) will hold a hearing to discuss and make a recommendation to the full Council on the above referenced appeal. The Committee hearing will take place in the Council Chamber, on the second floor of City Hall, 600 Fourth Avenue, Seattle, Washington. Adjudication of the appeal is a quasi-judicial action of the City Council and is subject to the Council's Quasi-judicial Rules. The Council's Quasi-judicial Rules were adopted by Resolution 31001 and are available at http://www.seattle.gov/council/legdb.htm.

Questions concerning the meeting or the Council's Quasi-judicial Rules may be directed to Ketil Freeman by calling (206) 684-8178 or via e-mail at ketil.freeman@seattle.gov.

Print and communications access for Council meetings is provided on prior request. Please contact LaTonya Brown at (206) 684-5329 as soon as possible to request accommodations for a disability.

CERTIFICATE OF MAILING

I certify under penalty of perjury under the laws of the State of Washington that on January 3, 2011, I sent the following documents: *Notice of Appeal Hearing* for the Controls and Incentives Appeal by 1507 Group L.L.C., for the Eitel Building, 1501 Second Avenue, to the following listed persons by first class mail, postage prepaid, at the addresses listed below, those addresses being the last known post office address or interoffice mail stop of each.

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ROGER WYNNE
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KAREN GORDON
DON
SMT-17-00

Signed this 3 day of January 2011 at Seattle, Washington.

(Signature)

Karl Fredrickson

(Printed Name)