

Case No. UNCT/13/2

UNDER THE UNCITRAL ARBITRATION RULES AND  
SECTION B OF CHAPTER 10 OF THE DOMINICAN REPUBLIC -  
CENTRAL AMERICA - UNITED STATES FREE TRADE AGREEMENT

BETWEEN:

SPENCE INTERNATIONAL INVESTMENTS, LLC, BOB F. SPENCE,  
JOSEPH M. HOLSTEN, BRENDA K. COPHER, RONALD E. COPHER,  
BRETT E. BERKOWITZ, TREVOR B. BERKOWITZ,  
AARON C. BERKOWITZ AND GLEN GREMILLION

Investors / Claimants

AND

THE GOVERNMENT OF THE REPUBLIC OF COSTA RICA

Respondent

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REPLY REPORT TO THE EXPERT REPORT OF Brent C. Kaczmarek, CFA dated July 15, 2014

Michael P. Hedden, MAI, CRE, FRICS

October 1, 2014

October 1, 2014

Tina M. Cicchetti, Esq.  
Fasken Martineau  
2900 – 550 Burrard Street  
Vancouver, British Columbia V6C 0A3

Re: Spence International Investments, et al. v. Republic of Costa Rica  
Case No. UNCT/13/2

Dear Ms. Cicchetti:

In fulfillment of your request, I have prepared my Reply Report to the expert report submitted in this matter by Brent C. Kaczmarek, CFA, dated July 15, 2014 (the "Kaczmarek Report").

FTI Consulting, Inc. ("FTI") has been retained by Fasken Martineau ("Counsel"), in connection with its representation of Spence International Investments, LLC, et al ("Claimants"). This Reply Report has been prepared for Counsel, in connection with its representation of Claimants for their use and distribution of the Reply Report is restricted to their use; the report may not be distributed to or relied upon by other persons or entities, except for the Government of the Republic of Costa Rica ("Respondent"), their Agents or the Arbitral Tribunal, without written permission of FTI. I reserve the right to update this Reply Report and any conclusions herein in light of additional information, research, or analysis that is provided to me.

Respectfully submitted,  
FTI Consulting, Inc.



Michael P. Hedden, MAI, CRE, FRICS  
Managing Director | Real Estate Solutions

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## 1 FTI Uses Industry Standard Accepted Methodology

On April 23, 2014, I provided my expert report valuing the Claimants' properties in Costa Rica (the "FTI Report"). I am a recognized, accredited real estate appraiser with over 30 years of real estate appraisal experience. The FTI Report was prepared using industry standard and accepted methodology with relevant and appropriate market information to conclude credible opinions of fair market value for the Claimants' property.

The Kaczmarek Report asserts that FTI's appraisal is flawed for three main reasons: 1) subjective adjustments to alleged comparable sales result in significantly divergent price points that are then averaged to conclude value; 2) the adjustments to the alleged comparable sales result in prices inconsistent with the market trends; and 3) reliance on alleged comparable properties did not account for purchasers' lack of due diligence. These assertions are without merit, as the Kaczmarek Report was not prepared by an accredited real estate appraiser, offers no alternative comparable sales data or analysis, does not attempt to use any industry recognized procedure or methodology to value the Claimants' property, and has no basis for determining the amount of knowledge that was possessed by buyers and sellers in the marketplace.

The Respondent has expropriated 75 m of beachfront property. For 15 of the Claimants' lots, this resulted in the taking of the entire lot. For these lots, the valuation is based on a sales comparison approach to determine the fair market value of each property on the valuation date. For the 9 other lots (the SPG and B lots), the Respondent has expropriate only a portion of each lot leaving the affected Claimants with a remainder property that is no longer beachfront or beach access. In the FTI Report, I also use a sales comparison approach with an industry standard accepted methodology to explain a simple economic concept to value the partial takings. Whether it's a road, a beach or any other amenities, the economic principle that the land fronting the amenity is more valuable than the land further from the amenity is a long-standing valuation theory.<sup>1</sup> In the instant case, the oceanfront part taken is worth more per m<sup>2</sup> than the part remaining that is further from the ocean. The Kaczmarek Report recognizes and accepts this economic premise that "lots closer to the beach will sell at a premium to lots that are further from the beach".<sup>2</sup> The FTI valuation for these lots values the part taken by comparing the value of the lot pre-taking with the value of the lot post-taking, as this is the accepted valuation methodology for a partial taking. Similarly, the goal of the valuation is to determine the fair market value of the property taken from the Claimants by the Respondent. As explained in the FTI Report, the taking of the beachfront portion of each property reduced the value of the remaining property, as it no longer had valuable beachfront contributing to its overall value.

### 1.1 Sales Comparison Approach Correctly Applied

FTI correctly applied the sales comparison approach in its expert appraisal report in valuing all of the subject properties. The challenge in any real estate appraisal assignment is to accurately report the actions of buyers and sellers in the marketplace using whatever market evidence is available. In this location of Costa Rica, obtaining verifiable retrospective market information from six years ago is extremely challenging. However, given the market information I received, I was able to confidently determine the fair market value for the subject properties as of May 2008.

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<sup>1</sup> Urban Land Appraisal; National Association Of Assessing Officers, 1940, p. 58

<sup>2</sup> See the Kaczmarek Report , paragraph 108

The Kaczmarek Report and I agree that the sales comparison approach is the most appropriate valuation methodology for the subject properties.<sup>3</sup> The Kaczmarek Report also acknowledges that the Costa Rican real estate market is not as transparent as the real estate market in North America.<sup>4</sup> The lack of transparency in Costa Rica makes the identification of comparable sales challenging. However, in my valuation experience of over 30 years, I have developed the acumen to decipher, analyze and conclude real estate values using the sales comparison method with whatever information the local market provides. The information that was obtained and analyzed was sufficient for me to conclude a credible valuation opinion of the subject properties.

## **1.2 FTI Used the Best and Most Relevant Sales Comparables Available**

The Kaczmarek Report does not attempt to conduct a sales comparison approach or offer any additional market information or superior comparables that could be used in the valuation of the subject properties. The criticisms from the Kaczmarek Report ignore the realities of the local real estate market.<sup>5</sup> Research indicated that there was a wide range of sale prices for similar properties within this market area. FTI considered comparable sales within an expanded time horizon to capture beachfront transactions considered to be the most important factor. The disparity between the resulting adjusted prices of the comparable transactions after market-based adjustments is symptomatic of the lack of transparency in the market. FTI used the best comparables that were available for consideration.

The lack of homogeneity and divergent prices amongst the sales sample is a function of the marketplace and a fact that cannot be ignored. Licensed and accredited real estate appraisers are trained to deal with inconsistent data. The adjustments I used in my analysis of the comparable sales are derived from analysis of market information, interviews with brokers and developers and are not overly subjective. The adjusted sales prices of the comparables were reconciled and weighted appropriately, FTI did not simply average as alleged by the Kaczmarek Report.<sup>6</sup> The sales comparison approach used by FTI results in a credible opinion of fair market value for the expropriated property based on all the evidence and analysis.

By contrast, the so-called fair market value conclusions in the Kaczmarek Report are not supported by any analysis and are inconsistent with other information relied upon in the Kaczmarek Report, such as: the final Costa Rican court awards, the Unglaube International Arbitration Award, and reported comparable sales.

## **1.3 FTI Uses Industry Accepted Rules for Partial Takings and The Larger Parcel Theory**

The Kaczmarek Report misconstrues the economic rationale for severance damage due to a partial taking of a property. This lack of understanding of the larger parcel theory is evidenced in paragraph 18 of the Kaczmarek Report whereby the criticism of the FTI Report focuses on the partitioning of the property being taken. The Kaczmarek Report analysis is contrary to recognized and accepted procedures because it does not recognize the value of the entire parcel and consider the loss of the most valuable

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<sup>3</sup> See the Kaczmarek Report , paragraph 13

<sup>4</sup> See the Kaczmarek Report, paragraph 22

<sup>5</sup> See the Kaczmarek Report, page 34, paragraph B

<sup>6</sup> See the Kaczmarek Report, paragraph 107

contributing portion of the subject property and its effect upon the remaining parcel.

The FTI Report uses the terms "Before Value" and "After Value" in the context of the alleged expropriation which are the appropriate, industry-standard terms used by real estate appraisers in this area of practice. The use of the terms "But-for" and "Actual" in the Kaczmarek Report are not used in real estate valuation treatises, indicate a lack of experience and are confusing in this context.

The methodology and valuation theory used in the FTI Report is universal in its application and is the industry standard valuation procedure.<sup>7</sup> The Federal Rule (before and after rule) has been developed to measure just compensation/damages in eminent domain litigation in the United States.<sup>8</sup> FTI has adopted the Federal Rule in this matter as the more thorough measure of analysis. Had FTI not followed the procedures dictated by the Federal Rule, the less analytic methodology, referred to as the State Rule, would have been utilized to just focus on the value of the part taken. Tony Sevelka, referenced in the footnote below, has written extensively on these valuation theories and their proper application for property expropriations in Canada which I consider to be applicable to the situation involving the Claimants' property.

Damages are calculated by valuing the property before the taking less the value of remainder property after taking. It is the property owner's right to receive the market value of the land taken and the before and after taking valuation methodology will account for the contributing value of the portion taken. Effectively, it is the amount that the property owner would have received for the part taken had it been sold on the open market on the valuation date.<sup>9</sup> As used in the FTI valuation of the SPG and B Lots, FTI uses industry accepted rules for valuation of partial takings in consideration of the larger parcel theory.

According to Black's Law Dictionary, a parcel taken through condemnation/expropriation is not a complete parcel but part of a "larger parcel," where the owner is entitled to damages from the severance as well as the value of the parcel taken. Partial takings that cannot be directly valued must have their value estimated as a function of the value of the larger parcel. This is the case when the part taken is not and cannot be a standalone parcel.. As a starting point, the "Before Value" of the whole parcel is used to determine a uniform unit value. It is the size of the larger parcel that exists before the taking and not the size of the taking that determines the unit value to be applied to the taking.<sup>10</sup> The functional relationship of the part taken to the larger parcel exemplifies the principle of contribution which holds that the value of a particular component is measured in terms of its contribution to the value of the whole property (larger parcel), or as the amount that its absence would detract from the value of the whole.

FTI correctly concludes that the highest and best use of the subject property is for residential development. Highest and best use is the reasonably probable and legal use of vacant land or an improved property that is physically possible, appropriately supported, financially feasible, and that

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<sup>7</sup> Uniform Appraisal Standards for Federal Land Acquisitions, Interagency Land Acquisition Conference, Washington, DC 2000, published by the Appraisal Institute

<sup>8</sup> Real Estate Valuation in Litigation, 2<sup>nd</sup> Ed. (Appraisal Institute 1995) at 23.

<sup>9</sup> Tony Sevelka, AACI,P.AA, "Parcel Taking Expropriation: The Remainder", Canadian Property Valuation (Volume 58/Book 1, 2014)

<sup>10</sup> Tony Sevelka, AACI,P.AA, "Parcel Taking Expropriation: The Remainder", Canadian Property Valuation (Volume 58/Book 1, 2014)

results in the highest value. Alternatively, the highest and best use is the probable use of land or improved property—specific with respect to the user and timing of the use—that is adequately supported and results in the highest present value.<sup>11</sup> In this case, either alternative supports the conclusion that the highest and best use is for residential development. The Kaczmarek Report offers no conclusion and ignores any consideration of highest and best use for the Claimants' properties.

The larger parcel, rather than the taking, is the entity for which highest and best use must be established and only then is it possible to estimate (indirectly) the value of the partial taking, which consists of the value of the land taken (calculated on the uniform unit value) and any severance damages suffered by the remainder parcel as consequence of the taking (lost contributing value of the more valuable part taken plus any damages from a change in highest and best use). The larger parcel establishes whether a claim for severance damages is applicable to the remainder parcel due to a change in utility. The underlying rationale is in recognition of partial takings that cannot stand alone as viable economic parcels and whose value is not directly ascertainable.<sup>12</sup> FTI adopts this rationale in the valuation of the B lots in consideration of the severance damage incurred by the partial taking.

#### **1.4 FTI Correctly Identifies and Calculates Severance Damages**

The FTI Report correctly identifies and calculates the severance damages applicable to the SPG and B Lots. FTI's conclusions accurately reflect the fair market value of the part taken when you add the pieces together. In other words, in determining the damages caused by the taking, one must consider the value of both the Part Taken and the Severance Damages. To consider the value of the Part Taken in isolation would fail to take into account the loss of the value of beach front and beach access property, which in the FTI analysis is built in to the Severance Damages.

Severance damages are generally used to mean those damages to a remainder property that are compensable. It is the decrease in value suffered by the remainder because of the taking of the more valuable portion of the land. In this case, the damage alludes not only to the loss of the value of the property in proximity to the beach (uniform price/m<sup>2</sup> for part taken plus contributing value) but also to the denial of beach access from the remaining lands which will require a drive to public access points, which is reflected in the lower price per m<sup>2</sup> of the remainder.

A non-marketable partial taking has no independent highest and best use so its value by necessity is a function of the value of the larger parcel. In terms of parcel size and utility, the larger parcel drives the selection of comparable sales and the comparative analysis of the sales comparison approach.<sup>13</sup> This issue specifically relates to the SPG Lots and the B Lots that would be entitled to compensation for the loss of utility of the remaining interior land (specifically parcels that cannot be individually developed as in remainder of the B Lots) as well as compensation for the partial land taken.

The Kaczmarek Report agrees with the concept of severance damages as described by FTI.<sup>14</sup> As defined in the Kaczmarek Report, severance damages are the difference between the "But-For" value and the "Actual" value. However, Mr. Kaczmarek demonstrates that he does not understand the concept of the

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<sup>11</sup> The Dictionary of Real Estate Appraisal, 5th ed. (Chicago: Appraisal Institute, 2010).

<sup>12</sup> Tony Sevelka, MAI, "Expropriation and Condemnation: The Larger Parcel", The Appraisal Journal (Spring 2008): 155-167

<sup>13</sup> Tony Sevelka, MAI, "Expropriation and Condemnation: The Larger Parcel", The Appraisal Journal (Spring 2008): 155-167

<sup>14</sup> See the Kaczmarek Report, paragraph 136

severance damage in a real estate context because of statements like the following: "it is entirely unreasonable..... that the portion of the SPG properties adjacent to the road..... would be equally affected by severance as those portions of the SPG properties immediately adjacent to the 75 meter strip"<sup>15</sup>. FTI's analysis captures the increased value of the remaining land in its new proximity to the beachfront. However, the loss in value of the more proximate beachfront land with direct access is equally spread throughout the remaining parcel. The Kaczmarek Report ignores the loss in value from denial of direct beach access and the greater distance from the ocean.

On pages 46 through 47, the Kaczmarek Report states that the comparable sales used and the methodology used to arrive at the "But-For" value and the "Actual" value were manufactured and illogical. (As previously discussed, the terms referencing the value are used by Kaczmarek and are not typical to real estate related matters.) However, FTI utilized beach front sales comparables when valuing the before taking and utilized interior lot sales comparables when valuing the after taking.

On page 7 of the Kaczmarek Report, it states that FTI's severance damage calculations were seriously flawed because comparable properties outside the 75-Meter Strip were utilized when calculating values for properties within the 75-Meter Strip. The Kaczmarek Report mischaracterizes "FTI's view". The interior sales in the "actual scenario" took into consideration the effect of the expropriation and the price paid for Lots A28, A29 and A30 reflected no impediment being constructed between the lot and the beach.<sup>16</sup> The photographs on pages 62, 64 and 66 of the FTI Report show the possibility of ocean views and sunsets and contradict the Kaczmarek Report's rationale that views are not possible.<sup>17</sup> In addition, the Kaczmarek Report does not consider the denial of direct access as part of the severance damage. The remainder properties are no longer either beachfront or even beach access.

The focus of arriving at the just compensation for the expropriation rests in the valuation of the best part of the Claimants properties. FTI's valuation methodology demonstrates that development within the 75-Meter Strip would yield higher values. When calculating real estate values for beachfront properties, beachfront property sales are the preferred sales comparables to use. The Kaczmarek Report wrongly asserts that the FTI logic assumes the views of the ocean and the beach for those remaining properties immediately outside 75 meter strip.

The Kaczmarek Report is wrong to assert that FTI did not submit any evidence that would indicate that the B Lots were restricted by zoning from building homes.<sup>18</sup> As submitted with my report, FTI Exhibit #38 is the zoning regulations for lots B1 through B8 and indicate a 5,000 m<sup>2</sup> minimum building lot requirement. Also, there are different zoning requirements between the SPG Lots and the B Lots and that explains why different lot sizes exist between the properties. FTI is correct to assert that the remaining B Lots are not standalone building lots. I note that the after taking valuation of lots B5 and B6 demonstrate this concept. The value of these remainders is higher, because I have concluded that the highest and best use is residential development. Despite the 5,000 m<sup>2</sup> minimum lot size, the remainder lots B5 and B6 share common ultimate ownership and my valuation assumes that these lots could be joined in order to create a legal building lot, albeit one without beachfront or beach access. I have

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<sup>15</sup> See the Kaczmarek Report, paragraph 143

<sup>16</sup> See the Kaczmarek Report, paragraph 55

<sup>17</sup> See the Kaczmarek Report, paragraphs 136 through 139 and Figure 10 on page 49

<sup>18</sup> See the Kaczmarek Report, paragraph 162



determined that the remainders of lots B1, B3, B7 and B8 also have value, as they could be combined with neighboring lots (not under common ownership) to create legal building lots. Of course, if the lots cannot be aggregated the remainder value is less (and the value of the part taken higher), as this would alter their highest and best use.

### **1.5 Development Valuation Model is Appropriate**

The Development Valuation Model (DVM) is appropriate in the analysis and valuation of SPG Lots 1, 2 and 3 combined. The Appraisal Institute refers to this analysis as the subdivision development method.<sup>19</sup> The DVM is a methodology only used to support the sales comparison approach and is not the primary approach used to estimate fair market value. It clearly demonstrates the contributing value of the beachfront lots to the larger parcel.

Despite the Kaczmarek Report's assertions, the details of FTI's DVM are evident on page 68 and transparent in the calculations on page 70 which can be replicated with a calculator.<sup>20</sup> Evidence relating to the subdivision and improvement cost estimates used in this analysis were submitted and disclosed as information relied upon in my report. Although severance damages are not "apparent" in the calculations, the result of the taking and the loss in value results from the \$10 million of lost revenue and resulting profit from the sale of eight beachfront lots with direct beach access. Unlike the methodology used for partial takings, the DVM methodology tolerates non-uniform m<sup>2</sup> pricing, as the property is valued as subdivided lots. The severance damages analogous to those in the partial taking analysis are partially incorporated into the higher per m<sup>2</sup> valuations (contribution of more valuable property to the development) and partially into the lost profit to the developer/owner from the sale of those more valuable lots.

Notwithstanding the Kaczmarek Report's criticisms, it is reasonably probable that the subdivision would have been approved and that a buyer would have reasonable expectation to assume its approval notwithstanding the environmental constraints of stress on the water system or aquifer.<sup>21</sup> The proposed development map shown on page 69 of the FTI Report was prepared by a licensed engineer and shows that the yield of 44 lots is physically possible given existing zoning regulations and is not highly speculative. The subdivision plan calls for eight beachfront lots.

### **1.6 FTI Applies a Market-Based Adjustment Process**

In the application of the valuation methodologies, FTI applied a market-based adjustment process throughout the report to all the Claimants properties. The Kaczmarek Report incorrectly states that "FTI arrives at the market value for the subject properties in each scenario by taking an average of three comparable sales".<sup>22</sup> The Kaczmarek Report mischaracterizes the calculations as averages when the sales are, in fact, weighted and reconciled to an indicated value conclusion.

The Kaczmarek Report states that FTI's market condition adjustment based on the application of the monthly inflation overstates the value.<sup>23</sup> FTI calculated market condition adjustments based on

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<sup>19</sup> Appraisal Institute, *The Dictionary of Real Estate Appraisal*, 5th ed. (Chicago: Appraisal Institute, 2010).

<sup>20</sup> See the Kaczmarek Report, paragraph 50

<sup>21</sup> See the Kaczmarek Report, paragraphs 128 & 129

<sup>22</sup> See the Kaczmarek Report, paragraph 53

<sup>23</sup> See the Kaczmarek Report, paragraph 112

monthly inflation factors correctly as shown on page 24 of the FTI Report. To demonstrate, Sale Comparable Lot 61 had a sale date of February 6, 2006. The effective date of value was May 27, 2008. The inflation factor used in the FTI Report was 3% per month in 2006, 1% per month in 2007 and 0% in 2008. Therefore, the value increased 33% in 2006, 12% in 2007 and 0% in 2008 for a total increase in value of 45% from the purchase date through the effective date of value. The resultant total appreciation is considered reflective of the market conditions during the time in question. Contrary to the FTI market evidence presented on page 24, the Kaczmarek Report offers no local market evidence to support the conclusion that "the market price is a real estate peaked in 2006 (just as they did in United States) and declined thereafter on a precipitous basis".<sup>24</sup> It is my opinion that the overall magnitude of adjustment to the comparables for market appreciation is reasonable based upon the market data and the paired sales analysis.

A Paired Sales Analysis was completed by FTI where the subject and comparable properties had similar characteristics such as location, physical features and beachfront proximity. The range in values resulted from market condition and size adjustments. The adjustment for interior to beachfront lots was developed by a paired sale analysis. Notwithstanding the size of the adjustments, the sales used were the best available in the marketplace (only verified transactions were used) and the Kaczmarek Report offers no contrary evidence to dispute FTI's factual evidence.

Comparable sales transactions were adjusted by as much as 121% upward and 70% downward. In Kaczmarek's view this is evidence that the comparable sales transactions do not have a high degree of comparability.<sup>25</sup> Kaczmarek noted that FTI's sales comparison analysis resulted in a wide range of values based on their alleged subjective adjustments. FTI used lots V52, V59 and V61 to value lots V30-V33, V32-V39, V40, V46-47 and V59.<sup>26</sup>

There were meaningful upward and downward adjustments primarily based on market condition adjustments where real estate values were increasing between 2-3% in value per month. There were size and locational adjustments as well which FTI considered credible and reasonable. Playa Ventanas and Playa Flamingo were judged to be better locations with better views and less vegetation. The adjustment for differences in location was confirmed by broker interviews and generally supported by market evidence and observation. The adjustment for size, location and physical features was seldom used throughout the valuation because it was not necessitated due to the similarity of the comparable transactions. Based on the analysis of sales data, it was evident that there was a wide disparity in the sales prices for what would appear to be very similar properties. I concluded this inconsistency was attendant to the lack of transparency in the marketplace. Using unfounded, subjective adjustments in the sales comparison approach to force a tighter range of the adjusted sales prices is inappropriate. Instead, the accepted approach is to opine to the reasonable, credible opinion of value based on the weight of all the evidence discovered. For this market, the major adjustment factor was related to market condition analysis, which was supported by the analysis.

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<sup>24</sup> See the Kaczmarek Report, paragraph 111

<sup>25</sup> See the Kaczmarek Report, paragraph 103

<sup>26</sup> See the Kaczmarek Report, paragraph 105

## 2 FTI Accurately Reflects Market Trends

FTI performed the appropriate research and due diligence to accurately conclude local market value trends. Kaczmarek states that according to FTI's appraisal of the subject properties, "...prices in Playa Grande a prices continued to rise in 2007 and 2008, contrary to the correlation with the U.S. market."<sup>27</sup> That statement is unfounded. The FTI Report showed the market appreciation slowing in 2007 to 1% per month and no appreciation in 2008. FTI utilized paired sales from the local Costa Rican real estate market in concluding market appreciation trends. Hence, the real estate sales data in Costa Rica told a different story than what was happening in the U.S. at the same time. Those sales were used when rendering market condition adjustments.

### 2.1 Participant Interviews

As part of the valuation process, FTI conducted several interviews with local market participants. The Kaczmarek Report refuses to give any weight to the letters from the real estate agents that are indicative of market sentiment.<sup>28</sup> Based on my personal interviews with the authors of the letters relied upon by FTI and as cited by Kaczmarek, I believe the letters to be truthful and an accurate reflection of market conditions as of the date of value. In contrast, Mr. Kaczmarek did not conduct any personal interviews and only relied upon media coverage without any corroboration.

The Kaczmarek Report notes that the letter from a local broker, Penelope Lent, indicates that from 2005 to 2008 she only sold one beachfront lot in the Playa Grande area due to concerns over the legal and expropriation risks upon the creation of the national park (FTI 10).<sup>29</sup> During my interview with Penelope she said that she continued to sell land in this area, as did others, despite her concerns and she confirmed that the values ranged from \$500/m<sup>2</sup> to \$1,000/m<sup>2</sup> during this time.

### 2.2 Use of Published Indices

FTI did not rely upon and believes it inappropriate for Mr. Kaczmarek to rely upon the Case-Shiller Index as a benchmark in the estimation of Claimants' property values. The Kaczmarek Report contends that Costa Rican real estate prices are correlated with prices in the U.S. According to Kaczmarek, Costa Rican real estate prices should follow the S&P/Case-Shiller U.S. National Home Price Index.<sup>30</sup> FTI agrees that real estate in Costa Rica is influenced by North American buyers but FTI does not agree that Costa Rican real estate prices should follow the S&P/Case-Shiller U.S. National Home Price Index. The Case-Shiller index is based on residential housing has nothing to do with land valuation trends in Costa Rica. Mr. Kaczmarek presents no support for his opinion and does not offer himself as an expert in the interpretation of residential housing trends or any real estate trends.

The S&P/Case-Shiller U.S. National Home Price Index is a composite of single-family home price indices within the United States for the nine U.S. Census divisions and is calculated monthly. It is included in the S&P/Case-Shiller Home Price Index Series which seeks to measure changes in the total value of all existing single-family housing stock.<sup>31</sup> The index was launched on May 18, 2006 and calculates the index

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<sup>27</sup> See the Kaczmarek Report, paragraph 15

<sup>28</sup> See the Kaczmarek Report, paragraph 164

<sup>29</sup> See the Kaczmarek Report, paragraph 83

<sup>30</sup> See the Kaczmarek Report, paragraph 29

<sup>31</sup> <http://us.spindices.com/indices/real-estate/sp-case-shiller-us-national-home-price-index>

in United States dollars with no specific weighting. The index aggregates the nine monthly U.S. Census division repeat-sales indices using a base and estimates of the aggregate value of single-family housing stock for those periods. The nine divisions are New England, Middle Atlantic, East North Central, West North Central, South Atlantic, East South Central, West South Central, Mountain and Pacific.

The S&P/Case-Shiller Home Price Indices Methodology states the following:

*"The S&P/Case-Shiller Indices are designed to measure, as accurately as possible, changes in the total value of all existing single-family housing stock. The methodology samples all available and relevant transaction data to create matched sale pairs for pre-existing homes. The S&P/Case-Shiller indices do not sample sale prices associated with new construction, condominiums, co-ops/apartments, multi-family dwellings, or other properties that cannot be identified as single-family. The factors that determine the demand, supply, and value of housing are not the same across different property types. Consequently, the price dynamics of different property types within the same market often vary, especially during periods of increased market volatility. In addition, the relative sales volumes of different property types fluctuate, so indices that are segmented by property type will more accurately track housing values."*

It is a well-known fact that real estate values are local in nature. There are differences in the economy and the forces affecting real estate values between a national residential real estate market index in the United States (i.e. Case-Shiller) and land values in Northern Guanacaste Costa Rica. A buyer in the U.S. real estate market can make a more informed investment decision because there is more readily available information and the volume of sales data is much higher. In my professional opinion, the use of this abstract index does not accurately reflect the value trends affecting the Claimants' property and therefore its use in the Kaczmarek Report is a meaningless analysis and conclusion.

### 2.3 Local Real Estate Market

The FTI Report relied upon information from the local real estate market in its estimation of the Claimants' property values. The Kaczmarek Report acknowledges and identifies rapid price appreciation.<sup>32</sup> However, the Kaczmarek Report offers no support for his contention that "When the market began to turn in 2007, buyers were caught holding properties they never intended to develop".<sup>33</sup> There is no support for the Kaczmarek Report's claim that most buyers were "flippers".<sup>34</sup> The market information that FTI discovered during its investigation indicates that many purchasers were looking to build vacation residences or second homes. There is no evidence of the predominance of speculators or "flippers".

The Kaczmarek Report suggests that FTI committed a fundamental error in their implementation of the sales comparison approach.<sup>35</sup> At paragraph 112 (Figure 3) of the Kaczmarek Report, the purchase price was appreciated by FTI's monthly inflation rate. Because this figure is lower than the fair market value determined by the sales comparison approach, the Kaczmarek Report alleges that FTI committed a fundamental error. This analysis might be relevant if the purchase prices were all at fair market value. Although the purchase price does not directly inform the fair market value assessment arrived at through a sales comparison approach, it would be logical for the same property to arrive at the same value by appreciating a fair market purchase price by market growth conditions. But the Kaczmarek

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<sup>32</sup> See the Kaczmarek Report, paragraph 40

<sup>33</sup> See the Kaczmarek Report, paragraph 41

<sup>34</sup> See the Kaczmarek Report, paragraph 15

<sup>35</sup> See the Kaczmarek Report, paragraph 112

Report forms no basis that the original purchase prices were reflective of market value. Instead, it claims that the "claimant purchases were speculative (and likely discounted)".<sup>36</sup> As a result, this analysis is nonsensical and inconclusive.

## 2.4 Selection of Comparable Sales

FTI selected and utilized the best available comparable sale information in the valuation of the Claimants' properties. Privately titled beachfront property in Costa Rica is rare. My research revealed few developments outside of Playa Grande that would have yielded additional comparable sales for use in the analysis. To the extent that such comparables were available, they were analyzed and considered and the appropriate locational adjustments made.

In addition, contrary to the allegations in the Kaczmarek Report that FTI did not adequately verify the comparable sales used in its valuation,<sup>37</sup> FTI used only verifiable transactions. The Kaczmarek Report acknowledges the Costa Rican real estate market is not as transparent as the real estate market in North America (as there are incentives for both buyer and seller to record a much lower than actual sales price) when it states: "Accordingly, data is not readily available to the general public surrounding the purchase and sale of real estate. As such, extensive research and analysis is required to understand the trends in the real estate market."<sup>38</sup> Understanding realities of documentation of transactions in Costa Rica, FTI used only verifiable transactions in their report, *i.e.* transactions where public records reflected the actual consideration reported and verified by the brokers.

It is not unusual for property sales contracts not to be available to appraisers and for FTI not to have them in its possession.<sup>39</sup> This practice was consistent with typical market behavior. The information discovered was sufficient for FTI to arrive at a well-supported opinion of value. As noted, the purchase price is not directly relevant to a valuation by sales comparison. This is especially the case when the purchase price reflects a bulk purchase of land that contains numerous lots, including the subject properties. I understand that this was the case for both the B lots and many of the properties owned by Spence Co.

Contrary to the assertion in the Kaczmarek Report, FTI appropriately selected the interior lots for comparison to the "actual" scenario in the after taking analysis. The value reflected by these sales (A28, A29, A30 and C71) considered the proximity to the beach and recognized that no building or other obstacle would be constructed between the lot and the beach, similar to the condition that will be experienced by the SPG and B lots in their after taking condition.

## 2.5 Use of Sales within the Las Baulas National Marine Park ("BNMP")

Proper valuation methodology for an expropriatory taking requires the valuator to ignore the impact of the expropriation scheme itself on the value of the property. Thus, the Kaczmarek Report's criticism<sup>40</sup> that the FTI Report does not consider the effect of potential expropriation is misplaced. My research indicated that the real estate market in Playa Grande was "hot" until late 2006 and early 2007 despite

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<sup>36</sup> See the Kaczmarek Report, paragraph 165

<sup>37</sup> See the Kaczmarek Report, paragraph 98

<sup>38</sup> See the Kaczmarek Report, paragraph 22

<sup>39</sup> See the Kaczmarek Report, paragraph 91

<sup>40</sup> See the Kaczmarek Report, paragraph 64

the stigma/cloud of potential expropriation that some local brokers referenced as early as 2005. Because of the shortage of verifiable comparable sales outside of the Park and because FTI was able to identify comparables within the Park (*i.e.* Lot V61) that were generally supportive of land values outside the Park, FTI's sales comparables are generally located within the Park. I consider the sales selected by FTI to be more appropriate than other sales made further afield that would have required more significant locational adjustments.

I note that had sales comparables been used from outside the Park, the values of the Claimants' properties would probably have been greater, as there would definitely not have been any stigma/cloud of potential expropriations. In my view, the comparable sales selected were the best available verifiable sales that did not require excessive subjective adjustment in order to make them comparable to the subject properties. Because these sales were used without an adjustment to account for the "scheme", they may, in fact, have resulted in an undervaluation rather than an overvaluation of the subject properties.

The Kaczmarek Report states that it was highly likely that Claimants would have obtained a discount in acquiring the subject properties.<sup>41</sup> Had the Costa Rican government's scheme permitted the claimants to purchase properties at a "discount", this fact would have to be ignored because of the government's continued and persistent interference in the marketplace and the significant value of oceanfront properties outside the BNMP. The Kaczmarek Report goes on to make the following totally contradictory statement "Therefore, FTI's use of comparable lots in the Playa Grande area would overstate the market value of the subject lots".<sup>42</sup> Comparing the two statements, the Kaczmarek Report appears to be claiming that properties in the area were purchased at a discount but using the comparables to value the Claimants property overstates the market value.

### 3 FTI Report Adopts Industry Accepted Definitions

FTI adopted accepted, industry-standard definitions in the preparation of their report. The following definitions of pertinent terms are taken from *The Appraisal of Real Estate, Fourteenth Edition* (2013) and *The Dictionary of Real Estate Appraisal, Fifth Edition* (2010), both published by the Appraisal Institute, as well as other sources.

#### 3.1 Market Value and Fair Market Value Standard

The market value standard used in the FTI Report is appropriate. FTI and The Kaczmarek Report agree that the standard of value to be applied in this case is "fair market value", as defined by DR-CAFTA, and the definition of market value used in the FTI Report comports with the generally accepted definition of fair market value.<sup>43</sup>

Market value is the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion (as taken from *International Standards, Eighth Edition*, published by the International Valuation Standards Committee).

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<sup>41</sup> See the Kaczmarek Report, paragraph 92

<sup>42</sup> See the Kaczmarek Report, paragraph 123

<sup>43</sup> See the Kaczmarek Report, footnote 32

The most probable price which a property should bring in a competitive and open market under all conditions requisite to a 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 is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

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

The fair market value standard is an objective standard based on the market not a subjective standard as to the assumed motivation of investors.

The Kaczmarek Report states that the Claimants knew or should have known that the land or portion of it was within the BNMP and that it is likely the purchase prices were discounted due to the risk that their purchases within the BNMP would ultimately be expropriated.<sup>44</sup> The Kaczmarek Report states that the sales of comparable properties does not take into account the fact that most purchases took place without proper due diligence and hence buyers' overpaying for their properties.<sup>45</sup> Without commenting upon whether these statements are supportable by the evidence, it is noted that, the Kaczmarek Report had previously stated that the properties were purchased at a discount. FTI is not an expert in terms of the Claimants' motivation or perception of value. FTI is an expert in real estate valuation based on a fair market value standard.

FTI provided an opinion of value on the real estate and not the rationale for the purchase of real estate by the Claimants. Paragraph 64 of the Kaczmarek Report wrongly claims that FTI assumes that Claimants did not know the properties could be subject to expropriation<sup>46</sup>. FTI's assumption as to what the Claimant knew or did not know is irrelevant to our valuation. Most importantly, any of the comparable sales that FTI used in establishing fair market value in our report assumed that buyers and sellers undertook the standard of care consistent with the local market custom. This is exactly the reason why the U.S. and Costa Rican real estate markets are not comparable and do not correlate. As previously stated, a buyer in the U.S. real estate market can make a more informed investment decision because there is more readily available information.

Therefore, it is my conclusion that the comparable sales used by FTI reflected the "fair market value" standard consistent with the criteria of "knowledgeable buyer and seller" encompassing proper due diligence.<sup>47</sup>

The Kaczmarek Report states that the Claimants' purchase of real estate was not on the basis of demand but on the assumption that real estate prices would continuously increase.<sup>48</sup> The Kaczmarek Report pointed out that one Claimant purchased lots in 2003 for US\$190 per m<sup>2</sup> and in 2006 for US\$685 per m<sup>2</sup> – a 261% increase. Buyers of real estate always assume that values will increase. No capital asset

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<sup>44</sup> See the Kaczmarek Report, paragraph 10

<sup>45</sup> See the Kaczmarek Report, paragraph 16

<sup>46</sup> See the Kaczmarek Report, paragraph 64

<sup>47</sup> See the Kaczmarek Report, paragraph 65

<sup>48</sup> See the Kaczmarek Report, paragraph 40

is purchased if there is an expectation for it to lose value. A measure of fair market value is the present value of future benefits.

In over 34 years of real estate valuation experience involving eminent domain (expropriation), I have never encountered the fair market value standard defined as the investors receiving their money back. For the Kaczmarek Report to suggest the proper approach is to "refund of their purchase price"<sup>49</sup> is absurd and beyond belief.

Fair market value (without taking into account the effect of the government's own measure on the value) is the standard of just compensation in this matter. Benchmarking against the purchase price and indexing without adequate proof that the Claimants' purchase price was based on a fair market value is neither an appropriate nor accepted valuation methodology. Mr. Kaczmarek is not qualified to determine whether or not the Claimants' purchase prices were equivalent to a fair market value and has performed no analysis to support this conclusion.

### **3.2 FTI Adopts Reasonable Assumptions Regarding Environmental and Entitlements**

FTI made reasonable assumptions regarding the environmental and entitlement issues affecting the Claimants' properties. In paragraph 127 of the Kaczmarek Report it states "if purchasers... were unaware of limited water supply ... all of the comparable sales referred by FTI would overstate the true fair market value of the subject properties". This is an assumption and pure speculation not voiced by any of the brokers or market participants that I interviewed. Based on conversations with local real estate brokers and the Claimants the highest and best use was for single family residential homes and there is no concern voiced regarding water or aquifer issues.

On page 37, Section 114, the Kaczmarek Report states that FTI assumes that highest and best use of the properties was for the construction and development of single family residential homes at Playa Grande and Playa Ventanas. Contrary to what is alleged at paragraph 125 on page 44, FTI made a reasonable assumption regarding water access and that there are no permeability issues with the aquifer. It should be noted that the Administrative Appraisals prepared for MINAE state that drinking water is available in close proximity to the SPG and B lots.

### **3.3 Interest Calculation**

It is beyond my scope of work as an expert in real estate valuation to opine on the basis of the interest calculation in this matter.

## **4 FTI's Alleged Discrepancies**

### **4.1 Purchase Dates**

FTI made best efforts to accurately report the Claimants' purchase prices and dates of acquisition. FTI did not simply rely on the Claimants' submission, but performed its own review and analysis of the registry and other legal documents, as well as interviews with third party sources in the market. In addition, FTI referred to the information in the Notice of Arbitration and Statement of Claim against the Government of the Republic of Costa Rica.

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<sup>49</sup> See the Kaczmarek Report, paragraph 165



FTI's research revealed that there was often a delay between what the buyer, the seller and the broker would consider the purchase date and the date of acquisition shown on the "Certificate of Property". This was made worse by the local custom of purchasing properties through the transfer of shares in a company rather than the immediate transfer of the property itself. Further, in a number of cases, the purchase price indicated on the Certificate of Property did not accord with the information provided by the brokers involved in the transactions. In most cases, the purchase price was indicated in dollars on the Certificate of Property and this was the currency used by the purchasers and brokers.

As illustrated in Table 6 (at paragraph 95 of the Kaczmarek Report), FTI generally used the date and purchase price shown on the Certificate of Property unless it was inappropriate to do so<sup>50</sup> or FTI had better information available from market sources.<sup>51</sup> In considering the Kaczmarek Report, FTI has revisited the data related to purchase dates and prices and makes the amendments set out in the following table.

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<sup>50</sup> For example, the purchase date identified on the Certificate of Property for Lot A40 is June 29, 2012. This is the date that the property was transferred to the State and not the date that Spence Co. purchased the property. Accordingly, for this property, the purchase date referenced in the Administrative Appraisal was used - June 2005. In addition, FTI recorded purchase dates of September 2000 for lots V39 and V40, as these were the dates on the Certificates of Property. However, lots V39 and V40 were purchased by Claimants through a share purchase in the company that owned these lots in September 2003. These types of transfer are not recorded on the Certificate of Property. This is another example of the purchase date on the Certificate of Property not accurately reflecting the actual acquisition date of the property.

<sup>51</sup> The Kaczmarek Report (page 18, footnote 44) noted that there was a discrepancy in the purchase date of C71 reported by FTI in Section 9.4 and Section 9.5. FTI reported a November 2007 purchase date based on its interview with Penny Wheeler, the real estate broker involved in the transaction. However, in the preparation of this reply report, FTI has reviewed the other documents related to Lot C71 and determined that the Claimants' purchase of this lot (as opposed to the date the Claimants sold this lot) occurred in February 2005.

<b>Lot</b>	<b>Date Used in FTI Report</b>	<b>Certificate of Property Date</b>	<b>FTI Reply Date</b>	<b>Notes</b>
<b>V32</b>	30 Sept 2003	30 Sept 2003	30 Sept 2003	No change
<b>V33</b>	30 Sept 2003	30 Sept 2003	30 Sept 2003	No change
<b>V39</b>	27 Sept 2000	27 Sept 2000	25 Sept 2003	Copher acquired these lots by purchasing 100% of the shares of Corporacion Lacheaven de Ventana, therefore the ownership change was not reflected on the certificate of property
<b>V40</b>	27 Sept 2000	27 Sept 2000	25 Sept 2003	
<b>V59</b>	3 Oct 2007	3 Oct 2007	3 Oct 2007	No change
<b>V61a</b>	6 Feb 2006	17 Feb 2006	4 Feb 2005	Certificate of Property reflects date of sale to third party not date of original purchase by Spence Co. Property purchased as one lot in 2005 and was subdivided into 3 lots in December 2006.
<b>V61b</b>	6 Feb 2006	15 Jan 2007	4 Feb 2005	
<b>V61c</b>	6 Feb 2006	15 Jan 2007	4 Feb 2005	
<b>A39</b>	29 Sept 2005	29 Sept 2005	29 Sept 2005	No change
<b>A40</b>	1 Sep 2005	29 Jun 2012	1 Sep 2005	No change. Administrative Appraisal states Sep 2005. Certificate of Property reflects date of transfer to State, not date of original purchase by Spence Co.
<b>C71</b>	22 Oct 2007	22 Nov 2007	4 Feb 2005	Ownership was acquired through sale of shares and mergers of various companies owned by Spence Co. in February 2005. October 2007 date was provided by real estate agent who transferred property on that date to a third party buyer (property subsequently returned to Spence Co.). Certificate of Property date reflect date of sale to third party and not the purchase date by Spence Co.
<b>C96</b>	11 Aug 2005	11 Aug 2005	11 Aug 2005	No change
<b>SPG1</b>	20 Dec 2006	11 Feb 2007	11 Feb 2007	20 Dec 2006 came from Bob Davey, Broker, however 11 Feb 2007 is used for consistency
<b>SPG2</b>	11 Feb 2007	11 Feb 2007	11 Feb 2007	No change
<b>SPG3</b>	11 Feb 2007	11 Feb 2007	11 Feb 2007	No change
<b>B1</b>	22 Sept 2003	22 Sept 2003	22 Sept 2003	No change
<b>B3</b>	22 Sept 2003	22 Sept 2003	22 Sept 2003	No change
<b>B5</b>	24 Sept 2003	24 Sept 2003	24 Sept 2003	No change
<b>B6</b>	24 Sept 2003	24 Sept 2003	24 Sept 2003	No change
<b>B7</b>	21 April 2004	21 April 2004	21 April 2004	No change
<b>B8</b>	24 Sept 2003	24 Sept 2003	24 Sept 2003	No change

In addition, FTI makes the following clarifications to the FTI Report.

<b>Lot</b>	<b>FTI Reference</b>	<b>Kaczmarek Reference</b>	<b>Kaczmarek Issue</b>	<b>FTI Response</b>
V59	Page 54	Page 32, Para. 96	Purchase price incorrectly stated at \$1,100,000	Typographical error. Correct purchase price of \$515,000 was stated elsewhere and used in the analysis. \$1,100,00 was a later list price for the property.
Lots V30 thru V34	Page 85	Page 13, Footnote 27	Bob F. Spence stated he purchased for approx. \$190 m2 in Aug and Sept of 2003	FTI Report stated a purchase date of August 2003 and price of \$182 m2. FTI Report's price and date is based on information received from Robert Davey, the real estate broker that handled the transaction. The variance is considered minor and immaterial.
Lots V39 and V40	Pages 50 & 51	Page 31, Para. 96	Purchase price incorrectly stated at \$500,000	Typographical error - should have read colons rather than dollars. \$340,000 purchase price in September 2003 cited by Claimants was confirmed by Robert Davey, the real estate broker that handled the transaction.
Lot V61	Pages 55,56,&57	Page 32, Para. 97	Purchase date incorrectly reported as February 6, 2006	Claimants' purchase price as \$800,000 in August 2005 as confirmed by Robert Davey, the real estate broker that handled the transaction. Claimant subsequently sold the lot for \$3.1 million, which was used as a comparable transaction (see FTI Section 9.5.5) for valuation purposes.
SPG2	Page 64	Page 31, Para. 95	Purchase price incorrectly stated at \$695,437	Typographical error carried over from SPG1 price. FTI report should have read \$1,004,563.
Lots A28, A29 and A30	Section 9.4 and 9.5, Pages 45 to 85	Page 19, Footnote 45	The adjusted values do not vary.	These are identical adjoining parcels that sold on the same date for the same price and therefore adjusted values should not vary.

<b>Lot</b>	<b>FTI Reference</b>	<b>Kaczmarek Reference</b>	<b>Kaczmarek Issue</b>	<b>FTI Response</b>
A40	Page 59	Page 31, Para. 95	Purchase date and price incorrectly stated as Sept. 1, 2005 for \$110,000	FTI used Administrative Appraisal as the source. However, Bob Davey verified date as Feb 22, 2005 for \$220,000, same as Lot A39.
Lots B1, B3, B5, B6 and B8	Section 9.4	Page 28, Footnote 80	Incorrect purchase price of \$500,000 per lot instead of 500,000 colons	FTI stands corrected. This transaction was not used as a comparable sale and the discrepancy does not affect the FTI value conclusion.

Notwithstanding these modifications, FTI notes that the slight discrepancies noted in the Kaczmarek Report<sup>52</sup> and corrected herein do not have any effect on the valuation conclusion in the FTI Report.

At paragraph 98 of the Kaczmarek Report, it states that the discrepancies between the dates of purchase and purchase prices “make it impossible to identify when Claimants actually invested in Costa Rica and the amounts that were actually invested.” I do not understand the date and amount of specific investments to be in any way relevant to the fair market value of the subject properties at the valuation date. In addition, the issues raised in the Kaczmarek Report on page 33, paragraphs 98 and 99 are also irrelevant to the FTI valuation as the relevant factors were identified and considered in the valuation analysis. The relevant sales data for the comparable properties were all verified. To be clear, unless the transaction is used as a comparable sale in the valuation process, the Claimants date of purchase and purchase price is irrelevant to the assessment of fair market value on the date of the expropriation.

## **5 Identification and Valuation of the Properties**

### **5.1 Not all properties are created equal**

At paragraph 120, the Kaczmarek Report states that the restriction of cutting down vegetation meant that property owners would not have beach front or ocean front views. The valuation of the subject properties in the FTI Report does not rely on the ability to clear vegetation in order to create unobstructed ocean views. As illustrated by the photos in the FTI Report, during my visit to the subject properties, it was clear that each of the subject lots had an ocean view and were beachfront. It was possible to access the beach from the subject properties through existing gaps in the vegetation. The lots on Playa Ventanas and North Playa Grande have no tall vegetation between the subject properties and the beach. The lots in South Playa Grande (the SPG and B lots) have taller vegetation between the subject lots and the beach. The better year-round views from the Playa Ventanas lots are reflected in the higher valuations for those lots. This does not mean that the lots in South Playa Grande do not have an ocean view. Figure 9 in paragraph 122 on page 43 of the Kaczmarek Report is a view with full vegetation in July and is quite different during the dry months. Notice the distinct difference between

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<sup>52</sup> The Kaczmarek Report, Table 6 on page 31.

the photo on page 71 of the FTI Report and page 43 of the Kaczmarek Report of the same property.

The Kaczmarek Report incorrectly identifies the vegetation as mangroves throughout the report. As noted in the Administrative Appraisals prepared for MINAE officials, the vegetation is in fact madero negro. Madero Negro is a medium size leguminous tree and it tolerates being cut back to crop height year after year.<sup>53</sup> The Kaczmarek Report is replete with wrongful identification of mangroves. There are no mangroves along the beachfront.

The Kaczmarek Report states (page 42, paragraph 121) that there were height restrictions on building in the Playa Grande area (although no source for this assertion is provided). Mr. Gremillion purchased his property in 2004 and had building plans for the construction of a two-story residence. I have identified several 2 story homes along the beachfront. The 2006 Zoning Regulations provided for 9 m height restrictions.<sup>54</sup>

FTI understood that these restrictions would still allow a 2-story structure, which would be sufficient to allow ocean views.

## 5.2 Local Administrative Findings

Mr. Kaczmarek is not qualified to make the statement in paragraph 161 that the "respondents appraisals appear reasonable" or in paragraph 167 "the administrative appraisals could be overstated in terms of fair market value" as he has no expertise, knowledge or performed the appropriate due diligence to make such a statement.

In addition, there is inconsistent logic in the Kaczmarek Report assertions that the Administrative Appraisals appear reasonable while at the same time the Kaczmarek Report contends that the Initial Purchase Price is the fair measure of compensation. Table 7 on page 56 shows that for some lots in Playa Ventanas, the Initial Purchase is greater than the Administrative Appraisal and in some cases the Initial Purchase is less than the Administrative Appraisal. In Table 8 on page 57 of the Kaczmarek Report shows that all the lots in Playa Grande are appraised at a fraction of their purchase price.

The acceptance of the Administrative Appraisal as indicative of fair market value is particularly difficult when you make a comparison between the Administrative Appraisals and the amount awarded by the Court. As shown in the chart below, the court awarded significantly greater than the Administrative Appraisal.

Lot	Administrative Appraisal	Court Award
A40	¢24,100,740.00	¢156,208,500.00
SPG 1	¢42,625,961.00	¢124,417,880.00
SPG 2	¢66,811,918.00	¢697,625,900.00
B3	¢19,978,421.00	¢120,417,880.00
B8	¢20,382,552.00	¢326,078,368.35

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<sup>53</sup> [http://en.wikipedia.org/wiki/Gliricidia\\_sepium](http://en.wikipedia.org/wiki/Gliricidia_sepium)

<sup>54</sup> [NTD: Add 2006 Municipality of Santa Cruz Zoning Regulations.]

However, the comparison of the administrative appraisal conclusions shown in Table 7 on page 56 with Table 8 on page 57 of the Kaczmarek Report is instructive. Comparing the oceanfront Spence Lot A40 in Playa Grande with Lot V30 in Playa Ventanas, the value differences are striking (\$51.91 per m<sup>2</sup> in September 2006 for A40 versus \$363.71 per m<sup>2</sup> for V30 in September 2008). It appears as though Playa Grande A40 is vastly undervalued considering the oceanfront location of this property. Additionally, the valuation of the remaining Playa Grande expropriated property in Table 8 appears, on its face, to be vastly below the value for any oceanfront property. Given this comparison, the administrative appraisals, on their face, do not appear credible to accurately/appropriately represent the fair market value of these properties.

FTI was not provided with the appraisals submitted by Claimant in appeal of Respondent's administrative appraisals<sup>55</sup>

### 5.3 FTI's Focus is on the Value of the Parts Taken

I have restated the FTI Report's findings to demonstrate the reasonableness of the valuation for the parts taken and consistency within the range of those values for the Claimants' properties.

Ownership	Location	Lot	Size m2	Total Value of Taking	Expropriated Value (\$ / m2)
Windows of the Blue Sky Net, SA	Playa Ventanas	V30	806.78	\$649,000	\$805
Windows of the Blue Sky Net, SA	Playa Ventanas	V31	839.53	\$676,000	\$805
Windows of the Blue Sky Net, SA	Playa Ventanas	V32	854.46	\$688,000	\$805
Windows of the Blue Sky Net, SA	Playa Ventanas	V33	913.71	\$735,000	\$805
Seize the Day, SA	Playa Ventanas	V38	1,076.93	\$867,000	\$805
Corporacion Lacheaven de Ventana, SA	Playa Ventanas	V39	1,011.80	\$814,000	\$805
Corporacion Lacheaven de Ventana, SA	Playa Ventanas	V40	856.87	\$690,000	\$805
Ronco Realty Investments, Ltda & Joeco Realty Investments, Ltda	Playa Ventanas	V46	935.05	\$753,000	\$805
Ronco Realty Investments, Ltda & Joeco Realty Investments, Ltda	Playa Ventanas	V47	1,154.49	\$929,000	\$805
Grande Beach Holdings, Ltda	Playa Ventanas	V59	892.58	\$718,000	\$805
Grande Beach Holdings, Ltda	Playa Ventanas	V61a	2,725.96	\$2,222,000	\$815
Grande Beach Holdings, Ltda	Playa Ventanas	V61b	889.58	\$748,000	\$840
Grande Beach Holdings, Ltda	Playa Ventanas	V61c	908.13	\$763,000	\$840
Grande Beach Holdings, Ltda	Playa Grande	A39	902.02	\$537,000	\$596
Grande Beach Holdings, Ltda	Playa Grande	A40	892.62	\$532,000	\$596
Grande Beach Holdings, Ltda	Playa Grande	C71	667.04	\$231,000	\$346
Grande Beach Holdings, Ltda	Playa Grande	C96	1,945.65	\$1,343,000	\$690
Keeping Track, Ltda	Playa Grande	SPG1	2,642.81	\$2,009,000	\$760
Keeping Track, Ltda	Playa Grande	SPG2	3,955.86	\$2,194,000	\$555
Keeping Track, Ltda	Playa Grande	SPG3	6,593.40	\$4,082,000	\$619
Aceituno Mar Vista Estates, SA	Playa Grande	B1	2,838.41	\$2,537,000	\$894
Guacimo Mar Vista Estates, SA	Playa Grande	B3	2,736.77	\$2,454,000	\$897
Pochote Mar Vista Estates, SA	Playa Grande	B5	2,879.18	\$1,965,000	\$682
Saino Mar Vista Estates, SA	Playa Grande	B6	2,773.95	\$1,947,000	\$702
Vacation Rentals, SA	Playa Grande	B7	3,012.20	\$2,556,000	\$849
Nispero Mar Vista Estates, SA	Playa Grande	B8	2,830.91	\$2,564,000	\$906

<sup>55</sup> See the Kaczmarek Report, paragraphs 158 and 159

## 6 Uniform Standards of Professional Appraisal Practice (USPAP)

I have certified that the analyses, opinions, and conclusions were developed, and the FTI Report was prepared, in conformity with the Uniform Standards of Professional Appraisal Practice (“USPAP”) and the Code of Professional Ethics and the Standards of Professional Practice of the Appraisal Institute. The Kaczmarek Report does not comply with USPAP or any real estate valuation standards.

In judging market trends in a retrospective value opinion, it's important to use only information contemporaneous with the value opinion. As used by the Kaczmarek Report, the market cycle in 2014 is not relevant to market values in 2008.<sup>56</sup> Value trends significantly past May 27, 2008 are irrelevant and consideration of any facts or information significantly after the date of value is not consistent with the Uniform Standards of Professional Practice.<sup>57</sup> The Kaczmarek Report is riddled with the benefit of 20/20 hindsight in articles and references that were authored well past the date of valuation.

The FTI Report also used post valuation date sales information in neighboring competing markets. However, the purpose was for informational purposes only as a confirmation of trends and to show that but for the Costa Rican's government interference in the Playa Grande and Ventanas real estate market, robust market activity would have occurred. To be clear, the post valuation date information in the FTI Report was not used in the valuation of the subject properties but only to show that the other local markets are generally reflective and supportive of the FTI value conclusions.

## 7 Certification

The undersigned do hereby certify that to the best of my knowledge and belief:

1. The statements of fact contained in this report are true and correct.
2. The reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions and are my personal, impartial, and unbiased professional analyses, opinions, and conclusions.
3. I have no present or prospective interest in the property that is the subject of this report and no personal interest with respect to the parties involved.
4. I have no bias with respect to the property that is the subject of this report or to the parties involved with this assignment.
5. My engagement in this assignment was not contingent upon developing or reporting predetermined results.
6. My compensation for completing this assignment is not contingent upon the development or reporting of a predetermined value or direction in value that favors the cause of the client, the amount of the value opinion, the attainment of a stipulated result, or the occurrence of a subsequent event directly related to the intended use of this appraisal.

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<sup>56</sup> See the Kaczmarek Report, paragraph 45

<sup>57</sup> The Appraisal Foundation, Uniform Standards of Professional Appraisal Practice, 2014-2015 Edition at U74 (Retrospective Value Opinions)

7. The analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the Uniform Standards of Professional Appraisal Practice and the Code of Professional Ethics and the Standards of Professional Practice of the Appraisal Institute.
8. The use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives. The subject lots were physically inspected by Michael P. Hedden, MAI, CRE, FRICS on February 11 through 13, 2014.
9. No one provided significant assistance to the persons signing this certification.
10. Other than the appraisal report identified in this report, I have not previously performed any other services as an appraiser or in any other capacity, regarding the properties that are the subject of this report. As of the date of this report, I have completed the requirements of the continuing education program of the Appraisal Institute.



Michael P. Hedden, MAI, CRE, FRICS  
Managing Director | Real Estate Solutions