

Damages Valuation of David Aven et al.'s Investments in Costa Rica

ICSID Case No. UNCT/15/3

by

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Supplemental Report



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I. INTRODUCTION AND EXECUTIVE SUMMARY

1. I have been asked by Vinson & Elkins RLLP (“Counsel”), representing David R. Aven, Samuel D. Aven, Carolyn J. Park, Eric A. Park, Jeffrey S. Shioleno, David A. Janney and Roger Raguso (jointly referred to as “Claimants”), to comment on Mr. Timothy Hart’s expert report¹ (“Hart Report”) related to the value of damages to Claimants due to Costa Rica’s blocking their real estate investments at their Las Olas Project, on May 12, 2011. I have only focused in this Report on certain issues raised by Mr. Hart in his April 5, 2016 report and Costa Rica’s Counter Memorial of April 8, 2016. Lack of response to any issue raised by Mr. Hart or Costa Rica should not be interpreted as acceptance of Mr. Hart’s or Costa Rica’s analyses or conclusions.
2. I estimated damages based on the fair market value principle, using a method suitable for pre-operational assets, which combines the value of Las Olas as a going concern (based on a DCF methodology, which represents the value of the project if it had been completed) and a real-estate appraisal value (which represents the value of the land and buildings, infrastructure if the project had not progressed any further than had been achieved as at May 12, 2011), and weights those two outcomes by the probability of business success. This methodology is widely supported by the financial literature.² Mr. Hart’s main contention with my methodology is that the component of value as a going concern is “...very difficult to accomplish for a pre-operational project with no historical performance metrics upon which to base or compare any projections.”³ This criticism, however, has no merit.

¹ See Expert Report of Mr. Timothy Hart, dated April 5, 2016, (hereafter, “Hart Report”).

² See Damodaran, A., “Valuing Young, Start-up and Growth Companies: Estimation Issues and Valuation Challenges,” Stern School of Business, New York University, May 2009 (CLEX-041). See also Koller, Tim, Marc Goedhart, and David Wessels. 2010. *Valuation: Measuring and Managing the Value of Companies*, 5th Ed. New York: John Wiley & Sons. pp. 697- 699, 717 (CLEX-084).

³ See Hart Report, ¶4.

3. First, I use actual listing price information from comparable mixed-use properties of lots, houses and condominiums in resorts located in the Puntarenas province of Costa Rica, in the same region where Las Olas Project was being developed. To further enhance the use of market comparables on Las Olas' revenue side, in this updated report I also use timeshare interval prices for Costa Rica, which I obtained from Resort Condominiums International (RCI).⁴
4. Second, the cost side of the real estate business poses no methodological challenges. The real estate industry is a well-established one, and my valuation model uses market information from comparable developments to estimate construction costs as well as profit margins for the different segments of the business. Finally, there is no difficulty in assessing a discount rate reflecting the business risks of operating in a mixed used real estate located in Costa Rica, as similar projects abound. The lack of historical performance data, therefore, is not an impediment to use the DCF methodology for this asset, even if at the time of its valuation (May 2011), it was at an infant stage.
5. Mr. Hart's second claim as it relates to my methodology is that a 68% probability of business success is "...completely speculative".⁵ This metric, however, is supported by more than 20 years of survey data on survival business rates collected by the Bureau of Labor and Statistics in the real estate and rental leasing industry, which provides useful and robust insight as to the probability of success of Las Olas as a going concern. Mr. Hart proposes no alternative metric for this parameter, whereas I pointed to evidence of similar projects that were completed in the Puntarenas area, including El Mistico and Malaga Residences, suggesting that in the absence of the measures the Las Olas Project had a high likelihood of being completed.

⁴ Resort Condominiums International (RCI) is the largest timeshare exchange company in the world with nearly four million members and approximately 4,500 affiliated resorts in over 100 countries. See RCI Timeshares Overview Webpage, Available at http://www.rci.com/pre-rci-en_US/explore-rci/about-rci/overview/rci-overview.page. (Last accessed August 1, 2016) (CLEX-085).

⁵ See Hart Report, ¶5.

6. Mr. Hart criticizes the appraisal value of the land as being “*inflated*”, allegedly because “...*the permits add no value if construction cannot be completed as planned.*”⁶ I find no merit to this criticism, since a willing buyer would adapt its construction plans to a different use or project, but knowing that the site had already been cleared permits for environmental and construction purposes. Furthermore, the land had already been developed, albeit partially, with infrastructure works with common-use features such as earthmovings to open up streets, urbanization cordons, as well as rainwater, potable water and electrical networks, all of which would unlikely reduce (rather than add) value, as Mr. Hart suggests.
7. Mr. Hart’s preferred methodology is to estimate damages based on the historical funds actually spent on Las Olas Project. Such a proposal, however, is not an accepted method to derive market value, as it fails to recognize the value at which the asset can be transacted, which seldom will be equal to the funds already spent on it.
8. Despite his methodological criticisms, Mr. Hart makes several observations and criticisms regarding the parameters I use in my DCF model, so as to determine the value of Las Olas as a going concern. There are a few observations made by Mr. Hart that prompted me to adjust or update certain parameters, whereas most criticisms prompted my responses, which are detailed in Section III of this report, but no changes on damages. The observations that prompted changes to damages are summarized below:
 - a. Based on new evidence I adjust the 10% discount on listing prices to derive transaction prices. The updated discount is slightly lower, at 7.8%;
 - b. I increase the average size of the lots to 649 m² using information from the master site plan⁷ rather than using an approximation of 600 m²;

⁶ See Hart Report, ¶5.

⁷ See Master Site Plan, September 2008 (CLEX-015).

- c. I now use timeshare price and financing terms sourced from RCI reports that are specific to Costa Rica. Using this new information, I increase the average down payment for timeshares from 15% to 30%, and decrease the average financing term from 10 years to 5 years. As well, instead of an average 16.9% interest rate, my model now uses a range of interest rates from the RCI reports of 16.8% in 2011 to 18.7% in 2014;⁸
 - d. I adjust the timeshare interval prices and marketing expenses to include expanded information from sources such as RCI, which publish data that is more specific to Costa Rica;
 - e. I correct minor computational errors in the estimation of the average lot price from REMAX and average house price for one of the market comparable properties, the Malaga Residences;
9. Table I below shows my updated damage valuation compared to my original one, valued as of May 2011.

⁸ See RCI, *Latin America and the Caribbean Vacation Ownership Factbook*, Mexico D.F, Mexico, 2011. pp. 40-47 (CLEX-086). See also RCI, *Latin America and the Caribbean Vacation Ownership Factbook*, Mexico D.F, Mexico, 2012. pp. 24-28 (CLEX-087). See also RCI, *Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean* Mexico D.F, Mexico, 2013. pp. 24-29 (CLEX-088). See also RCI, *Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean*, Mexico D.F, Mexico, 2014. pp. 33-37 (CLEX-089).

Table I Damages to Claimants' Investment in Las Olas as of May 2011

US\$ Million of May 2011		
	Original	Updated
(+) But-For Expected Value	74.4	69.6
Value of Going Concern (68%)	93.1	86.0
PV of FCFE		
<i>Lots</i>	15.5	17.8
<i>Houses</i>	22.2	21.8
<i>Condos</i>	24.4	25.6
<i>Timeshares</i>	23.5	13.0
<i>Hotel</i>	7.6	7.9
Value of Land (32%)	35.5	35.2
(-) Actual Value	0.4	0.5
Damages to Claimants as of May 2011	74.0	69.1

Source: CL Valuation Model – Second Report (CLEX-082)

10. To update damages from May 2011 to a current date, I had previously recommended using a prejudgment rate based on the cost of capital of the industry in Costa Rica, at an annual rate of 7.6%, compounded annually. In this report I include two alternative interest rates for consideration of the Tribunal: the first one is based on the commercial interest rate published by the Central Bank of Costa Rica on commercial loans in US dollars, which averaged 10% during May 2011 - May 2016.⁹ The second alternative derives a composite interest rate by combining the expected value of an update factor that gives a 68% weight to the 7.6% cost of capital (mimicking the probabilities of success of an ongoing concern) and a 32% weight to the update factor that I use to adjust

⁹ See Central Bank of Costa Rica, Interest Rate on Commercial Loans, 2011 – May 31, 2016. Available at <http://indicadoreseconomicos.bccr.fi.cr/indicadoreseconomicos/Cuadros/frmVerCatCuadro.aspx?idioma=1&CodCuadro=613> (Last accessed May 31, 2016) (CLEX-090).

real estate prices in Costa Rica (based on local inflation and movements in the foreign exchange rate). This alternative results in an average annual interest rate of 6.8% per year for May 2011- July 2016. The latter alternative provides the better fit with the characteristics of the asset in this case.

II. RESPONSES TO MR. HART'S CRITICISMS OF MY PRE-OPERATIONAL ASSET VALUATION EXERCISE

II.1 MY METHODOLOGY RECOGNIZES THE PRE-OPERATIONAL NATURE OF THE ASSET

11. Mr. Hart criticizes my valuation methodology that combines the value of the project as an ongoing concern with the value of the land appraisal in its current state weighted by the probability of occurrence of each scenario alleging it is inappropriate and flawed.¹⁰ Mr. Hart's main criticisms to my valuation methodology are centered on the following¹¹:
- a. That for the assessment of the ongoing concern using the DCF method it is very difficult to estimate forecasts with reasonable certainty for a project that does not have historical performance information;¹²
 - b. That the methodology to compute a 68% probability of success is "...*completely speculative*";¹³
 - c. That the appraisal value of the land is "*inflated*", allegedly because "...*the permits add no value if construction cannot be completed as planned*";¹⁴
12. Mr. Hart, however, does not offer any support for his allegations, neither from financial theory or valuation practice. In this section I will show that these criticisms to the

¹⁰ See Hart Report, ¶3.

¹¹ Mr. Hart also argues that arbitral tribunals and courts have regularly rejected claims for lost profits for pre operational companies due to the speculation in the calculation of the future values. Since I view this as an argument that involves a legal judgement, I offer no response to this criticism in this report. This should not be interpreted, however, as endorsing or agreeing with this statement by Mr. Hart. See Hart Report, ¶¶152, 163.

¹² See Hart Report, ¶¶ 4, 65, 106.

¹³ See Hart Report, ¶5. In connection to this probability of success, Mr. Hart also claims that in my methodology even if the business project is a failure, a third party would still pay for 68% of the cash flows that were never achieved. See also Hart Report, ¶ 162. This criticism fails to acknowledge that on, an *ex-ante* basis, the willing buyer would always pay for the expected value of the asset under success, weighted by its likelihood.

¹⁴ See Hart Report, ¶ 5.

methodology I use to value damages are unwarranted and, furthermore, that the valuation methodology I propose is substantiated both by financial theory and industry practice.

II.1.1 My Methodology is Consistent with the Financial Literature

13. In my original report I rely on the methodology set out in Professor Damodaran's 2009 article, where he lays the foundation for estimating the intrinsic value of a young company.¹⁵ The methodology he proposes is an application of a broader area of financial theory called the probabilistic approaches or scenario approach to DCF.¹⁶ Under this methodology, the asset is valued under a variety of scenarios, and then a probability is assigned to each scenario to estimate the expected value. This is exactly what the methodology I selected does in my assessment of value.
14. To estimate the fair market value given the pre-operational status of the asset as of May 2011, both the willing buyer and the willing seller would have to assess the probability that the project may become operational or that it would have to sell the land in the condition it existed just prior to the alleged measures by Costa Rica. If the business plan is to be successful, in turn, the value the buyer/seller can derive from that business takes into account both the additional investment costs to finalize the projects, as well as the future cash flows that can be expected via sales of real estate, condos and timeshares. Because these future cash flows bear risks, such cash flows are discounted at a risk-adjusted rate.

¹⁵ See Abdala First Report. Section IV.2. See also Damodaran, Aswath., *Valuing Young, Start-up and Growth Companies: Estimation Issues and Valuation Challenges*, Stern School of Business, New York University, May 2009. (CLEX-041).

¹⁶ See Damodaran, Aswath, *Probabilistic Approaches: Scenario Analysis, Decision Trees and Simulations*. Stern School of Business, New York University. Available at <http://people.stern.nyu.edu/adamodar/pdfiles/papers/probabilistic.pdf> (Last accessed June 19, 2016) (CLEX-091). See also Titman, Sheridan, and John D Martin. 2011. *Valuation: The Art and Science of Corporate Investment Decisions*, 2nd Ed. Prentice Hall. Section 3.3, pp. 58 -75. (CLEX-092). See also Koller, Tim, Marc Goedhart, David Wessels. 2010. *Valuation: Measuring and Managing the Value of Companies*, 5th Ed. New York: John Wiley & Sons. pp. 292-296 (CLEX-084).

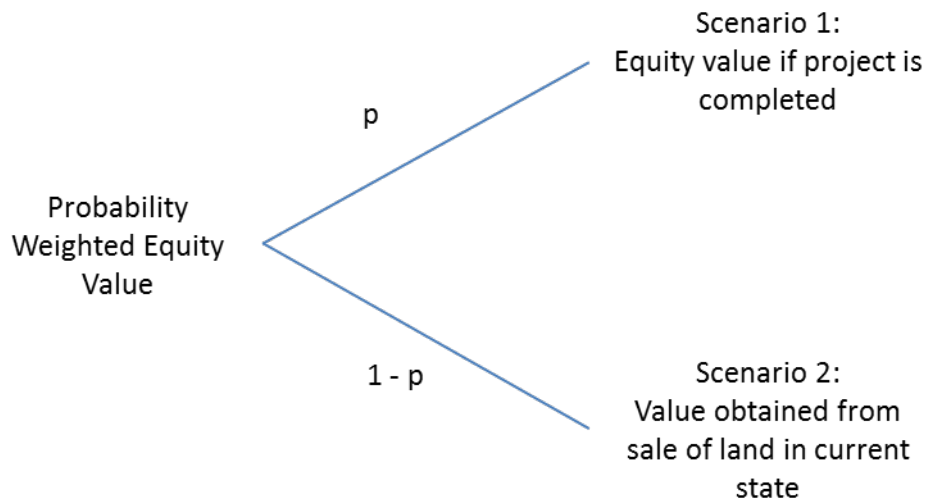
15. All businesses bear risks, however, and when Mr. Hart portrays that the cash flows are “uncertain”, what he really means, in economic terms, is that future cash flows are risky. Future cash flows, however, are risky not just for a buyer/seller of a pre-operational asset; they are also risky for a buyer/seller that is trying to transact the same asset, had this asset been already at operational stage. The pre-operational status, therefore, does not make the DCF method “less certain” or “more uncertain” as a method per se, as demonstrated by the fact that most young business and assets at pre-operation stage are typically valued using DCF methods.¹⁷ The only real difference in valuation analysis is that the hurdles that a pre-operational business has to face are higher than those of a business that is already operating. To adjust for such risk differential, the methodology that I use from Professor Damodaran assigns a probability of success. In practical terms, in my DCF valuation estimate, the pre-operational status of the business means that a willing buyer that would have expected to continue with the Las Olas development as of May 2011 would have paid 68 cents for every dollar of value that he would expect to earn from the business once it becomes operational.
16. Professor Damodaran also indicates that because this hypothetical willing buyer has the option to dissolve or discontinue the business, this means that such buyer could sell the land as is, rather than continue with the Las Olas development. In my methodology, therefore, the value of selling the (permitted) land has a probability of occurrence of 32%. This, in effect, covers the willing buyer’s “worst case scenario”: if it turned out on day one that they were unable to progress the Las Olas Project any further, the buyer would be able to re-sell the asset at this price.
17. Given the pre-operational nature of the asset, therefore, to estimate the expected value, the potential buyer would base his assessment on two mutually exclusive scenarios, in an

¹⁷ For further analysis of the use of the DCF methodology for pre-operational businesses, see Section II.1.2 of this report.

ex-ante basis. The first one is that the project is completed as envisioned in the latest available business plan for Las Olas (the December 2010 business plan) and the second one is that the project is not completed and the land is sold in its current state (*i.e.*, with the permits ready so that the potential buyer could undertake any other different real estate project).

18. For each scenario, I assess the value of the asset (using a DCF for the going concern scenario and a land appraisal approach for the non-completion scenario). I then weight each scenario for the likelihood of its occurrence. This can be summarized in the decision tree below:

Figure I Ex-Ante Decision Tree for the Willing Buyer



Source: Own production

19. The probability weighted equity value is thus the expected value that the potential buyer expects to obtain from purchasing the asset at its pre-operational stage and thus the value it is willing to pay.¹⁸
20. This methodology has various applications, in which rather than reflecting the risk in the discount rate it is explicitly modeled in the expected cash flows. Other authors apply this methodology when there are multiple choices of divergent scenarios. For example Koller et al. use it to incorporate the emerging market risk into a valuation and also to value high growth companies. Koller et al. state that even though valuing high-growth companies is challenging, “[t]he best way to value such companies is with a discounted cash flow (DCF) valuation, buttressed by economic fundamentals and probability weighted scenarios. Although scenario-based DCF may sound suspiciously retro, it works where other methods fail.”¹⁹ In this particular case, I use the methodology to account for the risk that the project is not completed, which is a risk that is not included in the discount rate.
21. Mr. Hart’s allegation is that under my methodology, even if the project is a failure, a third party would still pay for 68% of the cash flows that were never achieved.²⁰ This is incorrect because in such statement he confuses what a willing buyer/seller would pay *ex-ante* (before knowing whether the business will succeed or fail) with the *ex-post* valuation (once such buyer/seller knows for sure that the business would fail, as per Mr. Hart’s proposition). The value of the asset with its pre-measures status as of May 2011 is an *ex-ante* valuation as it relates to its operational outcome, since it assumes that neither

¹⁸ Pratt cites Reilly’s definition of the theory of valuation: “The value of an asset is the present value of its expected returns. Specifically, you expect an asset to provide a stream of returns during the period of time you own it. To convert this estimated stream of returns to a value for the security, you must discount this stream at your required rate of return.” See Pratt, Shannon P., and Alina V. Niculita. 2008. *Valuing a Business, The Analysis and Appraisal of Closely Held Companies*, 5th Ed. New York: McGraw Hill p.174 (CLEX-093).

¹⁹ See Koller, Tim, Marc Goedhart, and David Wessels. 2010. *Valuation: Measuring and Managing the Value of Companies*, 5th Ed. New York: John Wiley & Sons. p. 717 (CLEX-084).

²⁰ See Hart Report, ¶162.

the buyer nor seller know with 100% probability whether the project will be successfully completed or not, and therefore such potential buyer and seller would have to make their best estimates on what is the probability for each scenario, based on the information available.

II.1.2 No Speculative Elements: Hospitality Industry is Well-Established and Known

22. Mr. Hart's allegation that the lack of historical figures upon which to base my forecasts renders the results of my valuation speculative is unsubstantiated.²¹ The absence of historical performance figures does not prevent the cash flows to be estimated with reasonable certainty and does not render a valuation based on future cash flows inapplicable.
23. Neither Koller et al. nor Damodaran suggests abandoning the DCF methodology only because there is no historic performance on which to base the forecasts. Koller et al., refer to this in their chapter on the valuation of high-growth companies, which are similar to pre-operational assets in the sense that historical performance is either missing or unhelpful to forecast future cash flows. The authors suggest that when confronted with this situation, the valuation expert has to examine the expected long-term development of the company's market and then work backwards to estimate the company's cash flows.
24. In addition, Koller et al. suggest that since the long-term projections might be uncertain, it is best to create multiple scenarios.²² Professor Damodaran, for cases such as young companies where there is uncertainty on the long term development of the company advocates the use of the *top-down* or *bottom-up approaches*. The *top-down* approach is similar to the approach proposed by Koller et al. where the starting point is to estimate

²¹ See Hart Report, ¶65.

²² See Koller, Tim, Marc Goedhart, and David Wessels. 2010. *Valuation: Measuring and Managing the Value of Companies*, 5th Ed. New York: John Wiley & Sons. p. 717 (CLEX-084).

the market for a product or service and from there build down the estimates for revenues and cash flows. The *bottom-up* approach instead begins with an estimate of investment in capacity and then builds up to estimate the revenues and cash flows based on this capacity constraint.²³ The latter approach is the one I have used in my valuation.

25. In addition, authors such as Pratt also warn valuers that even though past history is relevant for projecting future economic income, it needs to be accompanied by an analysis as to what extent the forces generating future income will or will not duplicate the recent past. Pratt concludes that it is usually the case that history does not duplicate itself.²⁴ Therefore the mere existence of a history of performance does not mean that the future projections should be based on historic parameters, let alone that *only* historic parameters can support a future projection (the effect of Mr. Hart's complaint).
26. In my analysis, I forecasted cash flows for the assessment of the project as an ongoing concern based on market information for comparable properties for each segment that allowed me to construct forecasts of the cash flows associated with the model. The basis for my forecasts are:
 - a. The project definition of the 2010 business plans;²⁵

²³ See Damodaran, Aswath., *Valuing Young, Start-up and Growth Companies: Estimation Issues and Valuation Challenges*, Stern School of Business, New York University, May 2009. pp. 20-23, 28-29 (CLEX-041).

²⁴ See Pratt, Shannon P., and Alina V. Niculita. 2008. *Valuing a Business, The Analysis and Appraisal of Closely Held Companies*, 5th Ed. New York: McGraw Hill. p. 230 (CLEX-093).

²⁵ See Las Olas Business Plan, December 2010 (CLEX-016). Mr. Hart suggests that since the business plans have changed since the first one was prepared in 2004, these cannot provide a base on which to calculate lost profits. See Hart Report, ¶85. In the first place, I only use the business plan for the configuration of the project, I source my prices and costs as much as I can from public sources. Second, the updates on the business plan only show that the project would adjust to the most current business environment. Lastly, for my 2011 valuation, the business plan is still current since there have been no major changes in the Costa Rican real estate market (or, indeed, the US real estate market) between its preparation (December 2010) and the date of valuation (May 2011 – only five months later).

- b. Market information on listed prices for lot sales, house sales and rentals and condo sales and rentals in the Puntarenas province in Costa Rica, the area where Las Olas Project was to be developed;²⁶
 - c. Timeshare rental prices from listed prices as published in US reports and now updated with the availability of market information that is specific to Costa Rica, as published by RCI;²⁷
 - d. The determination of the investments necessary for the development of the lots, as per Mr. Calvo's assessments;²⁸
 - e. Public information on the construction costs for the houses, condos and timeshares in Costa Rica;²⁹
 - f. Industry reports and industry estimates on profit margins and other performance parameters;³⁰
27. Therefore, my forecasts, rather than being speculative as Mr. Hart states are market-based and extracted from public information available in the market for comparable assets. Just as a potential buyer would do in the absence of historic performance from where to source the parameters, I analyze multiple sources to form expectations on the cash flows the project would be able to generate if fully developed. I also note that even if Las Olas Project would have had a history of operations, and in line with Pratt's recommendation, my forecasts would have been contrasted with market comparables for

²⁶ The listed prices are for November 2015, as of the time when my first report was written. In the absence of a real estate price index, I converted listed prices from 2015 to 2011 using a general inflation index. *See* Abdala First Report, ¶¶ 87- 89, 93-95, 99, 103, 138-160.

²⁷ *See* Abdala First Report, ¶ 107.

²⁸ *See* Abdala First Report, ¶ 90.

²⁹ *See* Abdala First Report, ¶¶ 96, 104, 108.

³⁰ *See* Abdala First Report, ¶ 83.

any estimate of future cash flows, since market conditions cannot be solely or automatically extrapolated from historical performance.³¹

II.1.3 Changing Business Plans by Claimant Reflect Adaptation to the Market

28. Mr. Hart suggests that since the business plans have changed since the first one was prepared in 2004, these cannot provide a base on which to calculate lost profits.³² I disagree with Mr. Hart and find that the updates of the business plans only show that the project has been both evolving through time, and also adjusting to the most current business environment in order to obtain the highest value and do not render the last business plan unreliable. The willingness to adapt the Las Olas Business Plan to a new business environment is evident in Mr. David Aven's *Las Olas Project Overview September 2010*. In the executive summary, Mr. Aven acknowledges the fact that "We had to make some adjustments to the business model. Prior to September 2008 homes and condos were selling for about \$500,000 and our business model was geared to that price point. However, now the market price for homes and condos are in the \$250,000 range so we have to adjust our model to fit that reality. Therefore, we are adjusting our plans for the beach development and condo development for today's environment."³³
29. Las Olas management's ability to adjust to market trends is evident when comparing the objectives established in the 2004 Business Plan to the most recent December 2010 Business Plan. In 2004, management stated that its four primary goals for the Las Olas Project were to offer products and amenities to residents that embody high quality, security, a hacienda character, and a resort atmosphere.³⁴ In the 2010 Business Plan, Las Olas management maintained these four goals, but added "sustainability" and that Las

³¹ See Pratt, Shannon P., and Alina V. Niculita. 2008. *Valuing a Business, The Analysis and Appraisal of Closely Held Companies*, 5th Ed. New York: McGraw Hill. p. 230 (CLEX-093).

³² See Hart Report, ¶85.

³³ See Las Olas Project Overview September 14, 2010. p. 3 (CLEX-013).

³⁴ See Norton/EDSA Marketing Study, September 2004, Slide 12 (CLEX-006).

Olas would be a “*value oriented product*” by offering an “*exceptional beach property investment value to its buyers by being the best priced beach real estate product on the market.*”³⁵ As a consequence, even though the concept of the business plans has been slightly modified in size, pricing, and certain offerings over time, its essence of beach front residential vacation premises has not been altered.

II.1.4 Value of Las Olas as Going Concern

30. Following his criticisms of my valuation methodology, Mr. Hart turns his attention to the drivers of my going concern valuation for the Las Olas Project. After close inspection, I find that several of Mr. Hart’s comments to my key valuation drivers lack support or appropriate justifications and therefore require no adjustment to my valuation.³⁶
31. In the remaining sections of this chapter I address Mr. Hart’s criticisms on my estimation of revenues, costs, profit margins, and discount rates used to determine the value of the Las Olas Project as a going concern.³⁷

II.1.5 Revenues

II.1.5.a Costa Rican Real Estate Price Index

32. Mr. Hart has criticized my use of a retail domestic inflation index to adjust Costa Rica’s real estate listing prices from 2015 to 2011, alleging that “*real estate markets seldom track with retail inflation.*”³⁸ Mr. Hart does not provide support to his statement, but I would note that whereas real estate price inflation cannot be oblivious to the pace of general inflation in the economy, it is possible that there might be certain discrepancies

³⁵ See Las Olas Business Plan, December 2010, p. 11 (CLEX-016).

³⁶ For those comments prompting certain updates or corrections to my DCF going concern valuation, see Section III of this report.

³⁷ See Hart Report, ¶¶109 – 136.

³⁸ See Hart Report ¶110.

between the annual movement of real estate prices and domestic inflation. In the preparation of my original report I was unable to find any real estate price index that would show the price evolution of real estate properties in Costa Rica because such official price indices do not exist, something that Mr. Hart is aware of.³⁹ I was also unable to use other private or public sources, as I have not found any specialized outfit that would collect historic data on Costa Rica's real estate markets. For this reason I have calculated the 2011 prices using the using the general inflation index, adjusted by the devaluation rate, rather than a specific real estate index. This is the best approximation given the lack of information on real estate prices for Costa Rica. Mr. Hart does not suggest any alternative to this.

II.1.5.b Pricing of Lots

33. The emphasis of Mr. Hart's criticisms of my valuation of the lot sales for the Las Olas Projects relates to the price estimates employed in my model. For example, Mr. Hart criticizes that:
 - a. Using price information from a comparable resort, El Mistico, ignores Las Olas' own December 2010 business plan, which states that Las Olas is a unique property offering prices "at 50% to 70% below prices of its competitors";⁴⁰
 - b. The adjusted lot sales price, at US\$ 196 per m² is 35% higher than the price of actual Las Olas past lot sales between January 2008 and May 2011 at US\$ 146 per m² and

³⁹ I note that the first exhibit cited in Mr. Hart's report is a Global Property Guide article on property prices in Costa Rica. The first page of this report states that "Due to the absence of official house price statistics it is hard to assess the exact movements of house prices." See Lalaine C. Delmendo, "Costa Rica: stable property prices, rising foreign demand." Global Property Guide, September 30, 2015. p. 1 (CRED-01).

⁴⁰ See Hart Report, ¶112, See also Las Olas Business Plan, December 20, 2010. (CLEX-016).

77% higher than actual Las Olas past lot sales if only sales after 2009 are considered at US\$ 111 per m²;⁴¹

c. Five months prior to the valuation date, Las Olas management assumed sales of 100% of the lots at an average price of US\$ 60,000 in year 1, increasing at 3% annually, for a total of US\$ 21 million in sales. Given this projection by management, Mr. Hart suggests that it is unreasonable that lot prices in my valuation model are 62% higher than what management had hoped for five months prior to the alleged Measures.⁴²

34. Many of these criticisms by Mr. Hart on my pricing estimates for the lots at Las Olas, are based on comparisons to the December 2010 Business Plan for the Las Olas Project.

35. As explained, however, I do not base my pricing estimates on the business plan nor on past sales, but on market values that resulted from my own independent research. I find that this is more suitable to reflect the prices at which the project would be able to sell the lots, than what the management had forecasted.

36. My estimate average price for lots is based on information from “El Mistico Comunidad de Playa” (i.e., El Mistico) and information obtained from REMAX on listed prices for lots.⁴³ I find of particular interest the information from El Mistico, since this is a mixed use real estate development similar to Las Olas and is located only 9.4 km away from the Las Olas Beach Community as shown in Figure II.⁴⁴

⁴¹ See Hart Report, ¶113.

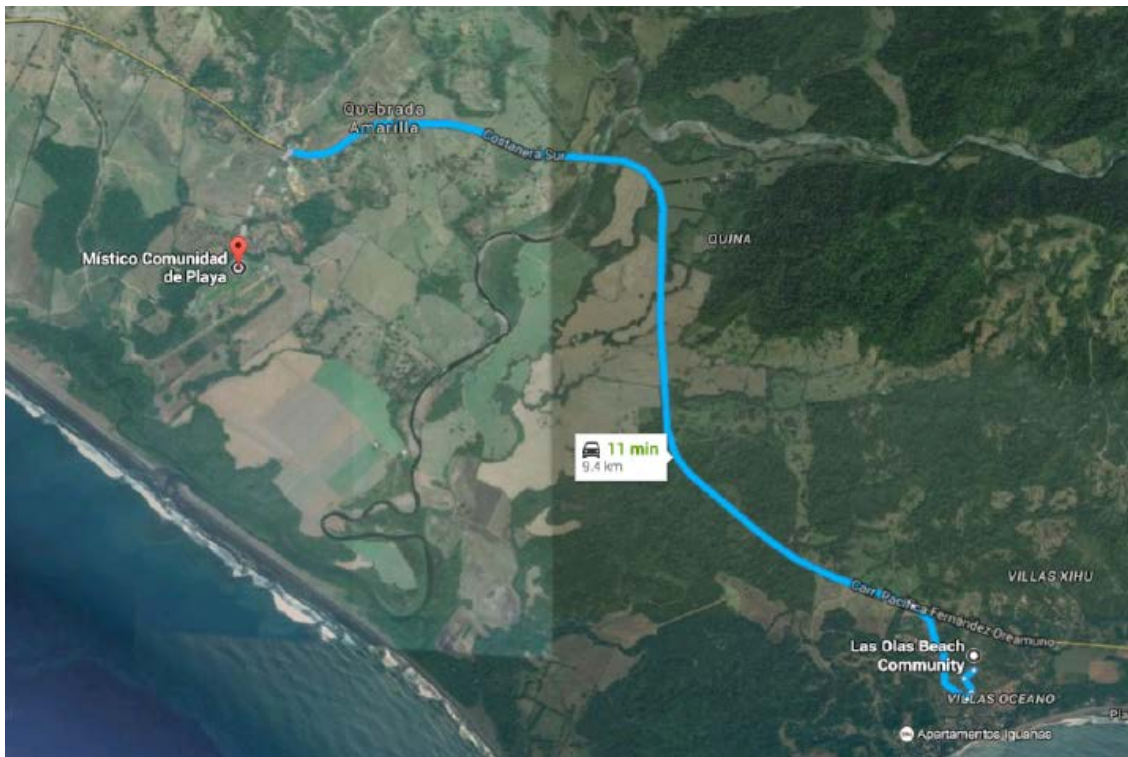
⁴² See Hart Report, ¶114.

⁴³ See Abdala First Report, ¶¶87, 138.

⁴⁴ For more on the configuration of the development see El Mistico Presentation, June 2016. Available at <http://online.fliphtml5.com/kdct/gnkp/#p=1>. (Last accessed June 25, 2016) (CLEX-119).

37. El Mistico is currently selling lots of Phase I⁴⁵ with immediate possession and of Phase II as pre-sale. The prices for these lots range between US\$ 210-255 per m² as of November 2015. Even though the size of the El Mistico lots are slightly smaller than Las Olas' (410-565 m² compared to 600m² for Las Olas), their price per m² provide a very reasonable and close parameter to the price at which Las Olas' lots would be selling for.⁴⁶

Figure II Distance between El Mistico and Las Olas



Source: Google Maps Search – Las Olas to Místico Comunidad de Playa (CLEX-114)

⁴⁵ Note that in El Mistico, 80% of the Phase I lots have already been sold, and Phase II has 16% of total lots sold. See El Mistico Presentation, June 2016, pp. 14 -15. Available at <http://online.fliphtml5.com/kdct/gnkp/#p=1>. (Last accessed June 25, 2016) (CLEX-119).

⁴⁶ See Email from El Mistico Sales Representatives, dated November 4, 2015. (CLEX-051). See also Abdala First Report, Table 4.

38. Notwithstanding, to make my sample more accurate, in my valuation model I also include lot price information from the REMAX lot listings in the area. The price obtained for this sample is not too different to the price of El Mistico at US\$ 202 per m².⁴⁷ I assume that given the market prices for lots in the area, Las Olas would have been able to sell the lots at a similar price, even though the business plans might have forecasted something else.

II.1.5.c Prices and Selling Terms for Houses

39. Mr. Hart's primary criticism related to my estimates of revenues generated from the construction and sales of houses is that I estimate the price of the constructed houses based on listed house prices and net out the value of the lot using my estimate of the value of the Las Olas lots.⁴⁸ Mr. Hart argues that in this way I am ignoring that the value of the empty lot (where the comparable house is to be constructed) may differ from the value of the Las Olas lots.⁴⁹
40. My approach to estimate the value of the constructed houses, however indirect, is needed since price listings do not specify the value of the lot and of the house separately. As a consequence I estimate the value of the constructed house as a residual value, by way of difference between the selling prices of houses, net of lot value.⁵⁰
41. In addition, Mr. Hart disputes my model's assumption that 90% of the lot owners would have paid Las Olas to coordinate their house construction. Mr. Hart claims that this

⁴⁷ See Abdala First Report, Tables 4, 12 and 13.

⁴⁸ See Abdala First Report, ¶93.

⁴⁹ See Hart Report, ¶121.

⁵⁰ Mr. Hart also suggests that the average price per m² from the Remax housing source in Table 15 of my report should be US\$ 1,783 (instead of my calculated value of US\$ 1,872), since the average house size is 279 m² and average house price is US\$ 497,401. This is, however, incorrect, as the value per m² of Table 15 is the result of averaging the price per m² of all properties included in the sample as I show in Table 14 of my report. Mr. Hart's calculation only divides the average house price by the average house size, which is less accurate. See Hart Report, ¶122. See also Abdala First Report, ¶151.

estimate is unsupported because it is based solely on the December 2010 Business Plan's projection that "90 % of Las Olas buyers are North American."⁵¹

42. The December 2010 Business Plan did anticipate that 90% of their target market would be from North America, which is a reasonable assumption as the Las Olas marketing efforts would have been concentrated in that segment.⁵² Given that the developer has a competitive advantage in terms of scale, since it will be building many houses at the same time in the location; it is likely it would be able to offer more comprehensive and bundled services than competing constructing companies.
43. Mr. Hart questions the assumptions my model uses to estimate the cash flows from the resale services of houses offered by the Las Olas Project; specifically that buyers would have, on average, held the properties for 10 years before selling. Mr. Hart speculates that the 10-year holding period estimate does not appear to have any basis.⁵³
44. My approximation of a 10-year holding period for houses and condos at the Las Olas Project is aligned with the median holding period statistics from the National Association of Realtors' Investment and Vacation Home Buyers Survey (2013). According to the NAR's U.S. survey statistics, the median length of time the buyers of vacation properties planned to own their property was 10 years, and the median estimate for buyers of investment properties was 8 years.⁵⁴ Given that 90% of the house and condominium owners at the Las Olas Project were projected to be from North America, the motivations of buyers and average holding period for properties would most likely follow the pattern observed at NAR's North American data. Thus, I find that my holding period for homes and condos of 10 years is a realistic and reasonable estimate for the Las Olas Project.

⁵¹ See Hart Report, ¶118 (i).

⁵² See Las Olas Business Plan, December 20, 2010, p. 23 (CLEX-016).

⁵³ See Hart Report, ¶118.

⁵⁴ See National Association of Realtors. Investment and Vacation Home Buyers Survey 2013, published April 2013. p.10 (CLEX-094).

II.1.5.d Prices and Selling Terms for Condos

45. Mr. Hart extends many of his criticisms related to parameters on the houses segment to my estimation of revenues from condominium sales, rental services, and resale services. For condominium sales, however, Mr. Hart notes that the starting selling price for condos in my model, at US\$ 265,880, is greater than the selling price stated in the December 2010 Business Plan, at US\$ 229,000.⁵⁵
46. Similar to the criticisms regarding lot and house prices and total sales, the comparison between my model's estimates and the Las Olas business plans is not suitable because I am relying on market listing prices for the units which I find more reliable than the business plan price estimates because they are based on actual market information.⁵⁶

II.1.5.e Timeshares Revenues from Financing

47. Mr. Hart criticizes the following features of my model's timeshare financing:
- a. That my estimate of timeshare revenues originated in the financing business has not been reduced by corresponding expenses incurred to provide timeshare services;⁵⁷
 - b. That my estimate of timeshare revenues does not account for non-collectible receivables;⁵⁸
 - c. That my forecast of timeshare revenues does not incorporate pre-payments of customers who have access to financing.⁵⁹

⁵⁵ See Hart Report, ¶126.

⁵⁶ See Abdala First Report, ¶83.

⁵⁷ See Hart Report, ¶132.

⁵⁸ See Hart Report, ¶132.

⁵⁹ See Hart Report, ¶132.

48. Mr. Hart's first criticism is incorrect. None of the documents I use as comparables have a separate expense related to the costs of the financing activities and I therefore have no basis to compute such costs separately from those already accounted for under overall sales and marketing expenses.
49. Second, in the case of non-collection, while it is true that there might be uncollectibles and that they are not explicitly modeled in my valuation exercise, it is also the case that in the timeshare industry, developers have the right to expeditiously liquidate the timeshare contract due to lack of payment. As a consequence, this may only imply a slight delay until a new buyer is found and the actual outcome of such anticipated liquidation of the contract could be that the overall revenues actually increase due to new sales, rather than decrease due to uncollectible receivables, As the JMP Securities report explains:

“Foreclosure or cancellation revokes the borrower’s ownership and access to the timeshare resort. This recovered inventory is eventually returned to the seller and resold through the normal timeshare sales process. The inventory recovery process for timeshares is fairly straightforward compared to traditional residential foreclosure. The most important distinction is possession. Timeshare owners, whether they own a traditional week-based interval or points, never physically possess the real estate. The timeshare company controls the keys and access to units. If an owner defaults on a loan, access to use the property is denied. This is much different than a residential foreclosure where homeowners eventually need to be physically dispossessed of the property and thus, avoids the physical degradation of property that is common during a residential foreclosure process. The timeshare owner simply loses access to the property and ownership and the interval or points are put back in the hopper and sold to the next buyer.”⁶⁰

⁶⁰ See JMP Report, JMP Securities, “Lodging: Timeshare Demystified – JMP’s Investor Guide to the Vacation Ownership Business,” January 23, 2014, p. 30 (CLEX-067).

50. Lastly, my model does not assume pre-payments or any related revenues that may be associated to pre-payments, such as pre-cancellation penalties. As with uncollectibles, I assume their effect would be neutral, since the pre-cancellation penalty can be calculated based on the income the project would not generate due to the pre-cancellation itself.

II.1.6 Cost Side

II.1.6.a Lots' Infrastructure Costs

51. Mr. Hart claims that although the Las Olas December 2010 Business Plan estimated that an additional US\$ 4.2 million of infrastructure costs would be needed to complete the construction of the lots for the Las Olas Project, my model does not account for any of these costs.⁶¹ This statement is incorrect as my model does account for infrastructure costs.⁶²
52. As with prices, I did not base my cost estimates on the business plan, but rather on the development budget prepared by the Engineer Manuel Calvo Navarro in October 2010 for the infrastructure costs necessary to convert the land into individual lots for sale.⁶³ The total budget for development costs according to Mr. Navarro's estimates is US\$ 8.9 million (as compared to the US\$ 5.7 million in the Las Olas December 2010 Business Plan).⁶⁴ Since a portion of these development costs (US\$ 2.9 million)⁶⁵ had already been incurred prior to 2011, in my model I assume that all additional infrastructure costs are incurred in the first year of development whereas sales are spread out, which is a conservative assumption, reducing the valuation. After subtracting the already incurred

⁶¹ See Hart Report, ¶115.

⁶² See "CAPEX" worksheet, cell (J67), CL Valuation Model. (CLEX-003).

⁶³ See Calvo Inspection Documents, p. 7 (CLEX-081).

⁶⁴ See Las Olas Business Plan, December 2010. p. 34 (CLEX-016).

⁶⁵ See Abdala First Report ¶¶ 32, 90. See also Calvo Inspection Documents, p. 7 (CLEX-081). See also Profit and Loss Statement Detail of Cotsco and Las Olas Capital, 2002-2011 (CLEX-022). See also "Appraisal" worksheet, CL Valuation Model (CLEX-003).

development costs, my model's remaining infrastructure cost total of US\$ 6.0 million, which is 30% higher than the US\$ 4.2 million estimate from the December 2010 business plan.⁶⁶

II.1.6.b Data Sources for Construction Costs

53. Mr. Hart claims that, when estimating construction costs per m², I should have used the quotes corresponding to the category of luxury construction prices.⁶⁷ The data source that I use to estimate the average construction costs for houses, condos, and hotels is based on an on-line private service provider based in Costa Rica⁶⁸, which reports that “*in most cases*” construction costs range between US\$ 430 per m² and US\$ 1,076 per m².
54. My model uses the average of this range, and excludes the two extremes of the lowest construction costs reported at US\$ 315 per m², as well as the luxury properties at a cost of US\$ 2,152 per m² or higher. The Las Olas Project was not designed to be constructed as a luxurious property, and therefore calculating construction costs based on the highest costs for luxury home categories, as suggested by Mr. Hart, is inappropriate.

II.1.6.c House & Condominium Rental Costs

55. Mr. Hart criticizes my house and condominium rental prices calculation by claiming that my model ignores all of the costs associated with renting the properties including cleaning, property management, and maintenance among others.⁶⁹
56. Mr. Hart's contention is not applicable since within the Las Olas Project the owner of each property is left responsible for the costs of cleaning and maintenance.⁷⁰ Therefore,

⁶⁶ See Abdala First Report, ¶90.

⁶⁷ See Hart Report, ¶¶119(i), 125, 135.

⁶⁸ See Costa Rica Real Estate Guide. Building Process Page. p. 2. Available at <http://costarica.com/real-estate/building-process/>. (Last accessed November 23, 2015) (CLEX-060).

⁶⁹ See Hart Report, ¶124.

I do not include any additional costs for rentals from my valuation because they would not be incurred by the project. The comparable sample projects from which I source the rental information do not include these rental services either; therefore there is no need to apply any adjustment for these service categories.⁷¹

II.1.6.d Timeshare Construction Costs

57. Mr. Hart criticizes the method that I use to estimate timeshare construction costs for common areas, claiming that, unlike other construction cost estimates elsewhere in my model, they are based on the Las Olas business plan.⁷²
58. This claim has no merit. To estimate the timeshare construction costs, I bundled both private and common areas to reach to a total average construction cost per unit of US\$ 96,649 as of May 2011.⁷³
59. To reach to this number, I use the same cost per m² I use to estimate construction costs for the houses and condominium segments from Costa Rican public sources.⁷⁴ To account for the cost of constructing common areas for the timeshare units, I first increase the construction cost per m² by 10%, which is the same method that I used for common areas in the condominium segment of the Las Olas Project.⁷⁵ Finally, so as to add common area elements that are not present in the condominium segment but that are part of the plan design on the timeshares units, I include the construction cost estimates for a

⁷⁰ See Las Olas Business Plan, December 2015, p. 12 (CLEX-016). Las Olas management states in its latest business plan that a “Property Management Company” would offer “maid and rental management services to property owners.” Thus, cleaning and maintenance costs would not be incurred by the project, and the property owners would have to source these services from a third-party.

⁷¹ See Remax Rental Properties, November 16, 2015, (CLEX-073).

⁷² See Hart Report, ¶133.

⁷³ See Abdala First Report, ¶108.

⁷⁴ See Costa Rica Real Estate Guide. Building Process Page. p. 2. Available at <http://costarica.com/real-estate/building-process/>. (Last accessed November 23, 2015) (CLEX-060).

⁷⁵ See Abdala First Report, ¶104.

clubhouse and a swimming pool, at a lump sum cost of US\$ 1.7 million, which is a figure that is sourced from the December 2010 Business Plan.⁷⁶

60. Therefore, in contrast to Mr. Hart's assertions, my model uses a consistent methodology to estimate construction costs across segments of the Las Olas Project, and separately takes into account the construction cost components that are exclusively related to the timeshares segment, such as the clubhouse and the swimming pool.

II.1.6.e Hotel Common Area Construction Costs

61. Mr. Hart suggests that my model does not include additional costs for construction of the common areas to the hotel segment of my valuation.⁷⁷ This statement is incorrect. In the same way I did with the condominium segment, I increase the total construction costs by 10% to account for an allocation of construction costs to common areas.⁷⁸

II.1.6.f Hotel Profit Margins

62. In the hotel segment to the Las Olas Project, Mr. Harts argues that the profit margin that I use to calculate the value of the hotel to the project has no justification and that this margin is solely based on a single source, coming from a benchmark of a proposed hotel in Panama.⁷⁹
63. Given that the stated intention of Las Olas' management was to build the 110,000 square foot hotel and sell it to a third-party, the developer would not be involved in the hotel's

⁷⁶ See Las Olas Business Plan, December 2010. p. 35 (CLEX-016). See also "CAPEX" worksheet, CL Valuation Model (CLEX-003).

⁷⁷ See Hart Report, ¶135.

⁷⁸ See "Segments" Worksheet, CL Valuation Model (CLEX-003).

⁷⁹ See Hart First Report, ¶136. Furthermore, Mr. Hart infers that it is not clear if the Panamanian hotel is even comparable to the hotel planned at Las Olas, and based on his research, that the benchmark hotel does not appear to exist today.

operation.⁸⁰ In my model, therefore, I assume that the sale of the hotel to a third party would have the same profit margin as the sale of constructed houses and condominiums.⁸¹

64. To further evaluate the use of my estimated profit margins, I now compute the implicit price value per room for the proposed hotel at Las Olas. The price value per room is a standard measure in the industry that allows comparison between transaction prices across different hotel assets of comparable categories, using the number of rooms as an approximation of asset size.
65. The profit margins that I use for the Las Olas hotel valuation implies a price value of US\$ 178,058 per room as of May 2011.⁸² This valuation per room can be compared to hotel sale transactions in Mexico and Central America. According to a HVS review of 14 hotel transactions in these regions that bear similar features to the proposed Double Tree Resort in Panama,⁸³ the average value per room was US\$ 228,324 per room and the median was US\$ 182,508.⁸⁴ The implicit value per room for the Las Olas hotel as going concern is 22% lower than the average and 2.4% lower than the median value per room of this set of comparables. Therefore, I find that my valuation for the hotel segment of the Las Olas Project as going concern to be a reasonable estimate.

⁸⁰ See Las Olas Business Plan, December 2010, p. 37 (CLEX-016).

⁸¹ See Abdala First Report, ¶115.

⁸² See Abdala First Report, ¶115.

⁸³ The data on these transactions are published in the HVS Self Contained Appraisal Report, p.122 (CLEX-069). In the report's section on the "Sales Comparison Approach" it presents a selection of comparable hotel sales within Mexico & Central America in the last five years. To generate the comparable sales list of 16 hotels, HVS "conducted a comprehensive search for transactions of hotels that bear comparison to the subject property in one or more key areas" The list also considers factors such as operational and physical similarities to the subject property, including brand affiliation and revenue-generating aspects.

⁸⁴ Own calculation based on data from Figure 11-3 of the HVS appraisal report. The "Hilton Mexico Portfolio Sale" transaction indicates the sale of three different Hilton properties in Mexico: (1) Hilton Garden Inn, Ciudad Juarez, (2) Hilton Garden Inn, Monterrey, (3) Hilton, Guadalajara in February 2010. The average value per room from the Hilton portfolio sale was US\$ 79,167. See HVS Self Contained Appraisal Report, p.122 (CLEX-069).

Table II Comparable Hotel Sale Transactions

Property	Location	Sale Date	Price	Rooms	Price/RM
			US\$ million	#	US\$ million
Hilton Mexico Portfolio Sale	Ciudad Juarez/Monterrey/Guadalajara	Feb-10	57.0	720	0.08
Four Seasons Mexico Distrito Federal	Mexico City	Oct-09	54.0	240	0.23
Samba Vallarta by Pueblo Bonito	Nuevo Vallarta, Nayarit	Jul-09	10.9	184	0.06
One & Only Palmilla Resort	San Jose del Cabo, Baja California Sur	Feb-08	157.5	172	0.92
Fairmont Pierre Marques	Acapulco, Guerrero	Oct-07	72.4	335	0.22
Fairmont Acapulco Princess	Acapulco, Guerrero	Oct-07	222.9	1,017	0.22
Le Meridien Cancun Resort & Spa	Cancun, Quintana Roo	Dec-06	75.0	213	0.35
Barcelo Tucancun Beach Resort & Villas	Cancun, Quintana Roo	Aug-06	38.0	332	0.11
Hilton Los Cabos Beach & Golf Resort	San Jose del Cabo, Baja California Sur	Apr-06	115.0	375	0.31
Barcelo Karmina Palace Manzanillo	Manzanillo, Colima	Mar-06	48.2	324	0.15
Casa de Sierra Nevada	San Miguel de Allende, Guanajuato	Feb-06	8.4	33	0.25
Camino Real Resort Loreto	Loreto, Baja California Sur	Dec-05	17.0	155	0.11
Barcelo La Jolla de Mismaloya	Puerto Vallarta, Jalisco	Nov-05	31.0	303	0.10
Barcelo Tucancun Beach Resort & Villas	Cancun, Quintana Roo	Apr-05	31.0	332	0.09
Average Value per Room					0.23
Median Value per Room					0.18

Source: Own production based on HVS Self Contained Appraisal Report p.122 (CLEX-069)

II.1.7 Discount Rate

66. In his report, Mr. Hart presents several criticisms to my chosen methodology to estimate the discount rate, as well as to certain parameters that I have used.⁸⁵ In the sections below, I address each of the criticisms related to the estimated discount rate.

II.1.7.aA Size Premium Is Not Appropriate

67. Mr. Hart argues that I should have included in my cost of equity a size premium to account for the Las Olas Project’s small size relative to the market and the comparable companies used in my beta calculation.⁸⁶ Although Mr. Hart provides no justification or support for the need of a size premium in the discount rate in the case at hand, the

⁸⁵ See Abdala First Report, Section IV.4.1.f and Appendix C. See also Hart Report, Section 8.2.3.

⁸⁶ See Hart Report, ¶141.

general theory behind the addition of a size premium to the discount rate is that smaller companies experience higher risk than larger companies, and consequently enjoy higher returns than larger firms.⁸⁷

68. There are several reasons, however, that indicates that the inclusion of a size premium to the discount rate is improper in this case. These are:
- a. The size premium is not supported by the CAPM (Capital Asset Pricing Model) theory;
 - b. Recent empirical studies find no supportive evidence for the presence of a size effect in smaller companies, especially since the 1980s;
 - c. The addition of a size premium is inappropriate in emerging markets, as relative size and characteristics differ from that of the U.S;
 - d. In emerging countries, the effect of small size, if any, might be already captured by the country risk premium.
69. Beyond the sphere of CAPM valuations, the so called “size effect” has also been found to be empirically unreliable across regions and time periods, and is also understood to reflect not the inherent effect of size, but rather of other underlying market risk factors. First, some authors have found empirical evidence that rejects the small size effect across regions (Fama and French 1998)⁸⁸ or in emerging markets (Barry et al. 2001),⁸⁹ while others have concluded that the size effect may actually be *reversed* in emerging markets, indicating that larger firms experience higher returns (Claessens, Dasgupta and Glen

⁸⁷ All else equal, including a size premium will increase the discount rate and reduce the valuation of the asset.

⁸⁸ See Fama, Eugene F., and Kenneth R. French. 1998. “Value versus growth: The international evidence,” *Journal of Finance*. 53 (6): 1975-1999 (CLEX-095).

⁸⁹ See Barry, C. Goldreyer, E., Lockwood, L., and M. Rodriguez. 2001. “Robustness of Size and Value Effects in Emerging Equity Markets, 1985-2000.” *Emerging Markets Review*. 3(1): 1- 49 (CLEX-096).

1998).⁹⁰ Second, there is evidence that the size effect varies over time. Brealey et al.,⁹¹ for example, found that the size effect has disappeared since approximately 1980. Similarly, Cochrane concluded, “You can see that not only has the small-firm premium disappeared [since 1980], the size-related variation in beta and expected return has disappeared.”⁹² Other authors, including Fama and French (2011),⁹³ find evidence that the long-term effect of size is weak or nonexistent. Finally, Damodaran (2012) observes that when the size effect is detected, it primarily comes from the so called “January effect,”⁹⁴ and thus concludes that firm size likely represents a proxy for other underlying risk factor(s).⁹⁵

70. The inclusion of a size premium for valuation purposes is therefore a contested issue among financial practitioners and academics. Professor Damodaran, for example, opines that the addition of a size premium to the CAPM as a means of adjusting returns not only violates the intrinsic principle of valuation of building up one’s model from fundamentals, but also lends itself to imprecision.

71. Professor Damodaran further states that:

⁹⁰ See Claessens, Stijn, Susmita Dasgupta, and Jack Glen. 1995. “The Cross-Section of Stock Returns: Evidence from Emerging Markets.” *Emerging Markets Quarterly*. 2 (4): 4 -16. (CLEX-097).

⁹¹ See Brealey, R., Myers, S., and Franklin Allen. 2006. *Principles of Corporate Finance*. 8th Edition. New York: McGraw Hill, pp. 196-197 (CLEX-098).

⁹² See Cochrane, John. 2001. *Asset Pricing, Revised Edition*. Princeton: Princeton University Press, p. 452 (CLEX-099).

⁹³ Fama and French also tested the momentum of returns and find strong momentum of returns (i.e., stocks that have done well over the past year will continue to do well) in all regions except Japan, as well as evidence that momentum of returns is stronger for small stocks. Fama, Eugene F., and Kenneth R. French. 2011. “Size, value and momentum in international stock returns,” *Journal of Financial Economics*. 105 (2012): 457- 472 (CLEX-100).

⁹⁴ The “January effect” refers to the observed phenomenon in which returns are higher in January of each year and the small size premium seems to be primarily observed in that month. Professor Damodaran explains, “eliminating that month from our calculations would essentially dissipate the entire small stock premium.” See Damodaran, A. 2012. “Equity Risk Premiums (ERP): Determinants, Estimation and Implications – The 2012 Edition.” Updated March 2012. *Damodaran Online*. p. 34 (CLEX-101).

⁹⁵ See Damodaran, A. 2012. “Equity Risk Premiums (ERP): Determinants, Estimation and Implications – The 2012 Edition.” Updated March 2012. *Damodaran Online*. p. 34 (CLEX-101).

“I have never used the Fama-French model or added a small cap premium to a CAPM model in intrinsic valuation. If I believe that small cap stocks are riskier than large stocks, I have an obligation to think of fundamental or economic reasons why and build those into my risk and return model or into the parameters of the model. Adding a small cap premium strikes me as not only a sloppy (and high error) way of adjusting expected returns but an abdication of the mission in intrinsic valuation, which is to build up your numbers from fundamentals.”⁹⁶

72. The inclusion of a size premium for an asset located in a developing market is particularly contested. As explained by Pratt (2009), an important court decision in the U.S. found that it made little sense to extrapolate Morningstar’s size premium to emerging markets and thus applied none. In particular, the Delaware Chancery Court ruled the following:

“The court, however, questioned whether size premiums developed for the U.S. market apply to foreign corporations. The court indicated that the valuation “...calls on the court to decide whether there is something inherently risky about the stock of companies that are small compared to their global competitors, or whether the small-stock premium arises only when a company is small in relation to the market on which it trades.” After conducting a review of the scholarship on this issue, the court concluded that a small-size premium “might well” apply to foreign companies in more highly developed markets, but would not apply at all (or to the same extent) to those in emerging markets.”⁹⁷

73. In sum, there is no support for the use of any size premium in this case and I thus do not include a size premium in my discount rate calculation.

⁹⁶ See Damodaran, A. Musing on Markets, “Alternatives to the CAPM: Part 2: Proxy Models,” April 29, 2011 (CLEX-102).

⁹⁷ See Pratt, S. (2009), Business Valuation Discounts and Premiums, 2nd Ed. John Wiley & Sons, p. 332 (CLEX-103).

II.1.7.b Leverage Should Be Based on the Industry's Typical Capital Structure

74. In the WACC calculation, the costs of financing through equity and debt are weighted by a capital structure. I apply the industry debt-to-equity ratio as the applicable capital structure to Las Olas.⁹⁸ Mr. Hart argues that this is incorrect because the capital structure for the Las Olas Project was 100% equity; Mr. Hart thus argues that I should have used the cost of equity as the discount rate (i.e., assuming an equity weighting of 100%).⁹⁹ Mr. Hart's argument, however, is inconsistent with the principles of fair market valuation.
75. Fair market value is generally defined as the price at which an asset would transact between a hypothetical willing buyer and a hypothetical willing seller, acting at arm's length, neither acting under compulsion to buy or sell and both having reasonable knowledge of the relevant facts.¹⁰⁰ Under this principle, therefore, the identity of the hypothetical willing buyer is unknown; thus, one cannot assume that the buyer would be a non-diversified investor (i.e., financing with 100% equity as Mr. Hart argues). Similarly, the hypothetical willing buyer could finance with debt, even if as of May 2011 the Claimant had thus far chosen to finance the developments with 100% equity.
76. As a consequence, my discount rate calculation is based on the optimal industry capital structure, which is consistent with the fair market value standard that I use in my analysis.
77. If one were to assume, as Mr. Hart does, that a willing buyer would have taken no future leverage (i.e., debt) for the Project, then the cost of equity would be the applicable discount rate. This cost of equity, however, should be calculated using what is called an "unlevered" beta, or a beta for a company with no debt. As of May 2011, I have

⁹⁸ See Abdala First Report, Appendix C.4.

⁹⁹ See Hart Report, ¶148.

¹⁰⁰ See Abdala First Report, Section IV.1.1 for a full discussion on the fair market value principle.

estimated an unlevered beta of 0.67,¹⁰¹ which results in an unlevered cost of equity of 8.3%.¹⁰²

II.1.7.c Other Discount Rate Parameters

78. Mr. Hart argues that I have improperly computed the risk-free rate, beta, country risk, and cost of debt parameters. I address each of these parameters in the next sections.

II.1.7.c.i Risk-free Rate

79. The risk-free rate represents the return on a portfolio that contributes no additional risk to the investor. To estimate this rate I use the average yield on the 10-year U.S. Treasury bond.¹⁰³ Mr. Hart prefers using a 20-year U.S. Treasury bond, citing to one academic source (Pratt (2014)).¹⁰⁴ A review of the financial literature, however, shows that the 10-year U.S. treasury bond is the most commonly used measure for the risk-free rate:
- a. Professor Damodaran uses the 10-year U.S. Treasury bond in his analysis of the market risk premium;¹⁰⁵ he has also explicitly stated that using the 10-year U.S. Treasury bond is sound practice in valuation;¹⁰⁶
 - b. Copeland et al. (2008) state that “...*the ten-year rate approximates the duration of the stock market index portfolio – for example, the S&P 500 – and its use is therefore*

¹⁰¹ See Abdala First Report, Table 19.

¹⁰² Discounted at an unlevered cost of equity, the value of the Las Project as a going concern would be worth US\$ 87.4 million as of May 2011, 6% lower than my original valuation.

¹⁰³ See Abdala First Report, Appendix C.2.1.

¹⁰⁴ See Hart Report, ¶143 and Pratt & Grabowski, *Cost of Capital: Applications and Examples*, 5th Edition, John Wiley & Sons, Inc. 2014 (CRED-15).

¹⁰⁵ See Damodaran, A. 2016. “Equity Risk Premiums (ERP): Determinants, Estimation and Implications – The 2016 Edition,” Updated March 2016. *Damodaran Online* (CLEX-104).

¹⁰⁶ See Damodaran, A. “What is the risk free rate? A Search for the Basic Building Block,” (2008), p. 10 (CLEX-105).

consistent with the betas and market risk premiums estimated relative to these market portfolios.”¹⁰⁷

c. Koller et al. (2010) explains that “*for U.S.-based corporate valuation, the most common proxy is 10-year government STRIPS.*”¹⁰⁸

80. There are other reasons to prefer 10-year bonds as a measure of the risk-free rate. Evidence suggests that 10-year U.S. Treasury bonds are more liquid compared to 20-year U.S. Treasury bonds. Longstaff (2004) computes the liquidity premium of these bonds over Refcorp (government) bonds (these are fully collateralized by Treasury bonds but not as liquid). Longstaff found that the liquidity premium of a 10-year bond is 13.13 basis points, compared to the 14.93 basis point premium of the 20-year bond and 16.28 basis point premium of the 30-year bond, suggesting that the 10-year bond is the most liquid of the three.¹⁰⁹ Thus, using 20-year Treasury bonds instead of 10-year Treasury bonds as a proxy for the risk free rate would add a liquidity premium producing a non-risk-based upward bias to the estimated cost of capital.

81. Finally, the 20-year Treasury bond has shown an historical pricing anomaly. According to widely accepted theories (especially the combination of “Pure Expectations Theory”

¹⁰⁷ See Copeland, Tom, Tim Koller, and Jack Murrin (1994), *Valuation: Measuring and Managing the Value of Companies*, 2nd Ed. New York: John Wiley & Sons, pp. 259-260 (**CLEX-106**).

¹⁰⁸ STRIPS are zero-coupon government bonds. See Koller, Tim, Marc Goedhart, and David Wessels (2010), *Valuation: Measuring and Managing the Value of Companies*, 5th Ed. New York: John Wiley & Sons, p.237 (**CLEX-084**). While the discount rate that I calculate is for a Costa Rica project, note that my methodology is based on estimating the cost of capital for a U.S. project and adding a country risk premium to account for the fact that the Project is located in Costa Rica.

¹⁰⁹ See Longstaff, F.A. 2004. *The Flight-to-Liquidity Premium in U.S. Treasury Bond Prices*, *Journal of Business*, Vol. 77, number 3, pp. 511-526 (**CLEX-107**).

and “Liquidity Theory”),¹¹⁰ the yield curve should have an upward slope.¹¹¹ However, 20-year Treasury bonds exceeded the yield of 30-year Treasury bonds for several years, thus raising concerns about their appropriateness as a measure of risk-free rates.¹¹²

82. For all of these reasons, I recommend the use of 10-year U.S. Treasury bonds in my estimation of the risk-free component of the WACC, consistent with standard valuation practices and the financial literature.

II.1.7.c.ii Beta Parameter

83. I estimate the Project’s beta using information on 176 companies classified as belonging to the Global Industry Classification Standard (*GICS*) 40403010 (“Diversified Real Estate Activities”), which includes companies engaged in a diverse spectrum of real estate activities including real estate development and sales, real estate management, or real estate services, but with no dominant business line.”¹¹³ Mr. Hart argues that I

¹¹⁰ The “Pure Expectations Theory” assumes that the various maturities of different bonds are perfect substitutes and suggests that the shape of the yield curve depends on market participants’ expectations of future interest rates. These expected rates, along with an assumption that arbitrage opportunities will be minimal, is enough information to construct a complete yield curve. The “Liquidity Theory” is an offshoot of the Pure Expectations Theory, and it asserts that long-term interest rates not only reflect investors’ assumptions about future interest rates but also include a premium for holding long-term bonds (investors prefer short-term bonds to long-term bonds), called the term premium or the liquidity premium. This premium compensates investors for the added risk of having their money tied up for a longer period, including the greater price uncertainty. As Medeiros de Morais (2008) explains it:

“According to the Pure Expectations Theory, no arbitrage conditions guarantee that long term interest rate is a good predictor of the future short term interest rate. In other words, the long term interest rate can be seen as a geometric mean of a series of short term interest rate. The Liquidity Preference Theory states not only that the long term interest rate reflects market expectations of the short term interest rate, but also that lenders demand a risk premium in order to lock in the interest rate for a longer period.”

See Medeiros de Morais, J.F., “The Determinants of Market Interest Rates in Brazil,” Institute of Brazilian Issues, George Washington University, Fall 2008, p. 16 (**CLEX-108**). See also Fabozzi, F. J. (2007), *Bond Markets, Analysis, and Strategies*, 6th Ed., New Jersey: Pearson Prentice Hall, pp. 116-122 (**CLEX-109**).

¹¹¹ The yield curve shows the relationship between interest rates and maturity.

¹¹² See Selected Interest Rates, Federal Reserve of St. Louis, Release H-15 (**CLEX-110**).

¹¹³ See Abdala First Report, Appendix C.2.3.

should have instead focused solely on companies in real estate development.¹¹⁴ Mr. Hart's argument, however, is conceptually incorrect.

84. In the scenario of Las Olas as a going concern, the project not only runs as a real estate developer, but also operates as real estate administrator, as well as a provider of various real estate services, including timeshares, financing, etc. As a consequence, the use of the industry benchmark of "Diversified Real Estate Activities," is appropriate.

II.1.7.c.iii Country Risk Premium

85. The country risk premium is the additional risk premium to account for the fact that the Project is not located in the U.S. I base my estimate of the country risk premium on the spread of Costa Rica Government Bonds over the 10-year U.S. Treasury bonds, which are representative of a risk-free rate.¹¹⁵ Mr. Hart argues that my country risk premium estimate should have used the 20-year U.S. Treasury bond rate instead of the 10-year U.S. Treasury bond rate. Mr. Hart's argument is flawed for several reasons:
86. First, as I explained above in Section II.1.7.c.i, the 10-year U.S. Treasury Bond is a better measure of the risk-free rate than the 20-year U.S. Treasury Bond;
87. Second, the Costa Rica Government Bonds that I relied upon have 10 years to maturity as of the respective valuation dates; using a risk-free rate measure based on the 20-year U.S. Treasury bond would thus distort the measure of the spread as the comparison between yields would include factors other a representation of country risk premium (e.g., maturity risk).

¹¹⁴ See Hart Report, ¶145.

¹¹⁵ See Abdala First Report, Appendix C.2.4.

II.1.7.c.iv Cost of Debt

88. My cost of debt estimate is based on a synthetic approach that adds to the risk-free rate the country and industry risk faced by lenders with debt stakes in projects such as Las Olas.¹¹⁶ Mr. Hart argues that my cost of debt calculation is inappropriate because of the same reasons he prefers to use alternative measures of risk-free and country risk premium estimates. The responses to the criticisms to the risk free rate and the country risk premium are already presented in Section II.1.7.c.i and II.1.7.c.iii above.
89. Mr. Hart also disagrees with my estimate of the industry premium on debt, arguing that my industry premium estimate is “unsupported.”¹¹⁷ For this input, I use the average industry premium provided by Professor Damodaran for all real estate related industries: Housebuilding (2%), Property Management (2.5%), and Real Estate Investment Trust (REIT) (1%) industries for my May 2011 discount rate calculation.¹¹⁸ As I explain in Section II.1.7.c.ii when discussing the industry beta, the Las Olas Project, as a going concern, includes activities related to real estate development (i.e., “Housebuilding”), real estate administration (i.e., “Property Management”), and various real estate services (i.e., “REIT”). Thus, the use of the average of the real estate related industries provided by Professor Damodaran (resulting in a 1.8% industry premium as of May 2011) is appropriate.

II.2 LAND APPRAISAL VALUATION

90. Mr. Hart criticized my valuation of the land in its current state on the following grounds:

¹¹⁶ See Abdala First Report, Appendix C.3.

¹¹⁷ See Hart First Report, ¶147.

¹¹⁸ For my November 2015 discount rate calculation, I use the same source (Professor Damodaran) but slightly different industries due to reclassification: Real Estate Investment Trust (1%), Real Estate (Development) (1%), Real Estate (General/Diversified) (1%), and Real Estate (Operations & Services) (1.5%).

- a. The appraisal I use from Mr. Calderon as a basis for the valuation was prepared before the 2010 business plan;¹¹⁹
 - b. To adjust the timing of the data I used a general inflation index rather than an index that would take into account changes in the real estate market conditions;¹²⁰
 - c. There is no cost analysis to account for the partial urbanization adjustment.¹²¹
91. None of these criticisms is substantiated nor does it change my valuation. Mr. Calderon's assessment was prepared under the asset approach methodology. This means that the land appraisal was based on comparable pieces of land as of 2009, not on a particular business plan. Therefore Mr. Calderon needs not to be aware of the completion of the 2010 Business Plan or any other business plan.
92. With respect to the indexation mechanism that I use to adjust Mr. Calderon's market comparables as of 2009 to re-express values as of May 2011, there is no official index on the evolution of real estate prices in Costa Rica, and as a consequence I apply retail inflation as an approximation. See further explanations on this at section II.1.5.a of this report.
93. Finally, even though I do not perform a cost analysis, in adjusting Mr. Calderon's urbanization estimates to account for its partial development, out of all the expenses categories already incurred in the project I only include the ones described as construction costs specifically, which constitute 41% of the costs already incurred in the project.¹²²

¹¹⁹ See Hart Report, ¶155.

¹²⁰ See Hart Report, ¶156.

¹²¹ See Hart Report, ¶157.

¹²² See Abdala First Report, ¶32.

II.3 THE 68% SUCCESS RATE IS WELL SUPPORTED BY STATISTICAL AND LOCAL EVIDENCE

II.3.1 The 68% Success Rate Is Based on Broad Statistical Evidence of Survivorship

94. The 68% probability rate that I apply to weigh the “successful project” outcome, in which the Las Olas Project becomes a commercial enterprise, is based on direct data from the Bureau of Labor Statistics (*BLS*) for private businesses operating in the real estate and rental and leasing sector.¹²³
95. This data shows that there is a 51% probability that such a business will survive to its sixth year of operations based on the average sixth year survival rate for companies starting business in every year between 1994 and 2009 (i.e., the last year with data available for the 6-year survival rate). From the total of companies which did not survive (49% of the sample), however, there are companies that closed operations for both voluntary and involuntary reasons. To compute a measure of business success, therefore, one has to adjust the 51% by adding the number of business exits that were explained by voluntary reasons (which could have been originated in a merger, or in a personal decision by the owner to be accept employment elsewhere, or in retirement, among other motives).¹²⁴ Headd (2003), using data from the U.S. Census, showed that 34% of U.S. business closures are voluntary.¹²⁵ Adjusting the 51% survival rate with the BLS results on voluntary closings produces a 68% probability rate of success.¹²⁶

¹²³ According to the North American Industry Classification System (*NAICS*) code 53. The NAICS is the standard used by Federal statistical agencies in classifying business establishments for the purpose of collecting, analyzing, and publishing statistical data related to the U.S. business economy. Available at <http://www.census.gov/eos/www/naics/>. (Last accessed June 1, 2016).

¹²⁴ See Headd, Brian, 2003. “Redefining Business Success: Distinguishing Between Closure and Failure,” *Small Business Economics* 21: p. 52 (CLEX-002).

¹²⁵ See Headd, Brian, 2003 op. cit. pp. 51-61 (CLEX-002).

¹²⁶ Probability rate = BLS Survival Rate + ((1-BLS Survival Rate)*34%), or: 68% = 51% + ((1-51%)*34%).

96. Mr. Hart argues that the 68% probability rate is “*speculative and unsupportable*” due to the following arguments:¹²⁷
- a. The BLS data is based on U.S. data and is thus not comparable to the business environment in Costa Rica;
 - b. The six-year time periods of the BLS survey that I use and the data on which Headd (2003) relies are not comparable to the time period during which Las Olas was pre-operational.
97. Although data on survival rates on real estate industry that would be specific to Costa Rica would be preferable to assess Las Olas’ probability of success, such data, in the form and granularity presented by the BLS, is not available for Costa Rica.
98. A 2014 report on Costa Rica published by Global Entrepreneurship Monitor, and based on research prepared by the University of Costa Rica, the Chamber of Industries of Costa Rica, and ParqueTec, contains a breakdown of reasons why entrepreneurs discontinued their business. The breakdown shows that while the single-most cited reason for closure is low profitability (46%), 47% of closures were because of voluntary reasons.¹²⁸ This is slightly higher than the 34% voluntary closure rate from Headd (2003) that I use to adjust my probability rate.¹²⁹
99. Mr. Hart also argues that the data that supports the 68% probability rates are from time periods not comparable to the time period during which Las Olas was pre-operational.¹³⁰

¹²⁷ See Hart Report, ¶7 (viii), 149.

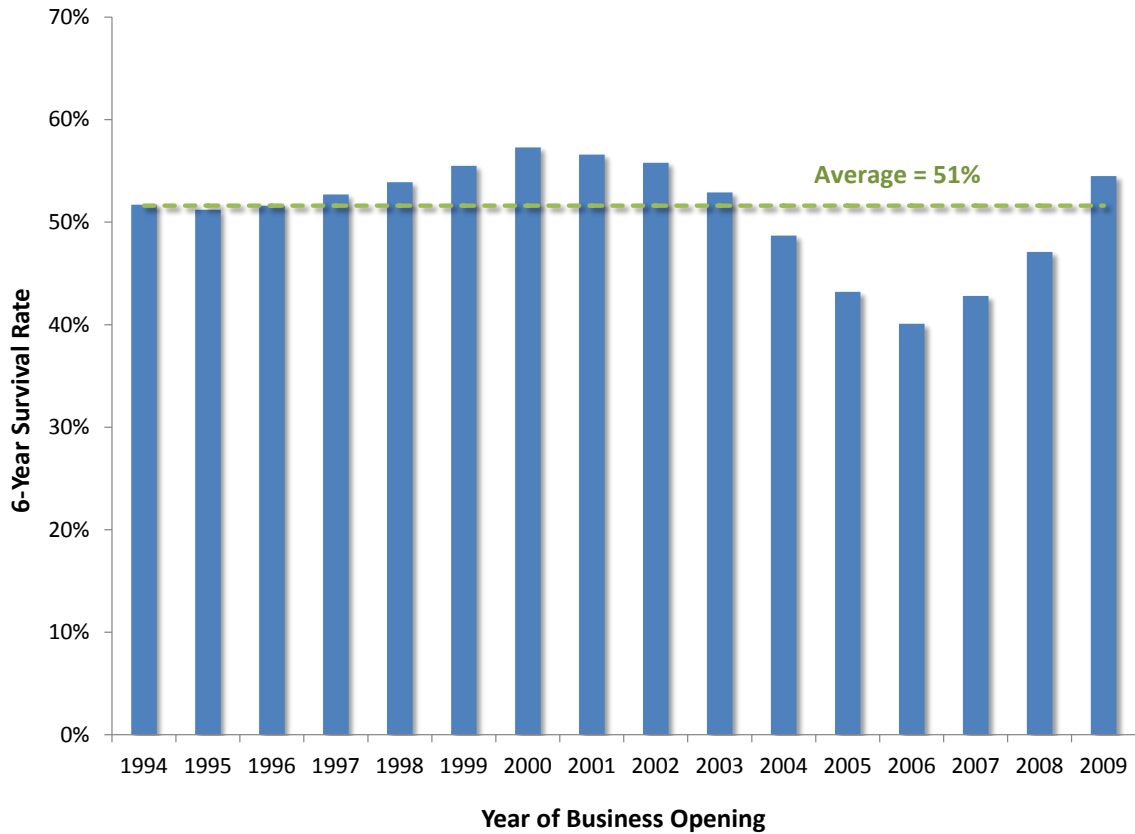
¹²⁸ The voluntary reasons include opportunity to sell (4.08%), retirement (2.04%), planned exit (5.1%), starting another job or business (4.08%), and personal reasons (31.63%). The involuntary reasons include accident (1.02%), sales issues (6.12%), and low profitability (45.92%). See 2014 Global Entrepreneurship Monitor (GEM) Report, p. 27 (CLEX-111).

¹²⁹ Even though this provides more support to my estimated percentage of voluntary closings, I do not apply it to the survival rates since these are based on US statistics, and it would be preferable in this case to avoid the combination of the two sources.

¹³⁰ See Hart First Report, ¶150.

This is not the case. First, the 6-year survival rate per the BLS is very consistent across time. Figure III below plots the 6-year survival rate for companies starting their business each year between 1994 (the first year with data available from the BLS) and 2009 (the latest starting date with data available for a 6-year survival rate). Figure III shows, for example, that a company starting its business in 1994 had a 52% chance of maintaining operations for at least six years. While the 51% survival rate that I use in my analysis is based on the average of all starting years, the 6-year survival rate is very consistent across the period, decreasing to a low of 40% for business starting operations in 2006 but otherwise within a tight range of 50%. Additionally, the 51% average is consistent with the most recent data published by the BLS, which shows that businesses beginning operations in 2009 had a 55% chance of surviving for at least 6 years.

Figure III 6-Year Survival Rate - BLS



Source: BLS Industries at a Glance. Real Estate and Rental and Leasing. (CLEX - 048)

II.3.2 Evidence of Successful Comparable Resorts in the Proximity

100. In order to assess the likelihood of success of the project I also analyze the evolution of similar developments in the area. In my original report I mentioned several similar developments cited in the 2004 Norton/EDSA report.¹³¹ Below I provide more detail of three developments that are located in the vicinity of Las Olas.

¹³¹ See Abdala First Report, Section III.2.2.

II.3.2.a.i *El Mistico Comunidad de Playa*

101. El Mistico is a mixed use real estate development¹³² similar to Las Olas and is located only 9.4 km away from the Las Olas Beach Community as shown in Figure II. As previously mentioned in this report, El Mistico is currently selling lots of Phase I¹³³ with immediate possession and of Phase II as pre-sale. The prices for these lots range between US\$ 210 - 255 per m² as of November 2015. The sizes of the El Mistico lots are slightly smaller than Las Olas' (410-565 m² compared to 600m² for Las Olas).¹³⁴

II.3.2.a.ii *Residencias Malaga*

102. The Malaga Residences are located in Playa Punta Bejuco, which similar to El Mistico is only 9.5 km away from the Las Olas Project.¹³⁵ The resort is a mixed use development offering 220 m² lots, houses, and apartments for sale.¹³⁶ Malaga has three different models of houses to choose from ranging in sizes of 68 m² to 90 m² depending on the model type.¹³⁷ As of 2016, the resort had completely sold out of its Modelo Classico house model.¹³⁸

¹³² For more on the configuration of the development see El Mistico Presentation, June 2016. Available at <http://online.fliphtml5.com/kdct/gnkp/#p=1>. (Last accessed June 25, 2016). (CLEX-119).

¹³³ Note that 80% of the Phase I lots have been sold and 16% of the Phase II lots. See El Mistico Presentation, June 2016, p. 14 – 15. Available at <http://online.fliphtml5.com/kdct/gnkp/#p=1> (Last accessed June 25, 2016) (CLEX-119).

¹³⁴ See Email from El Mistico Sales Representative, dated November 4, 2015 (CLEX-051).

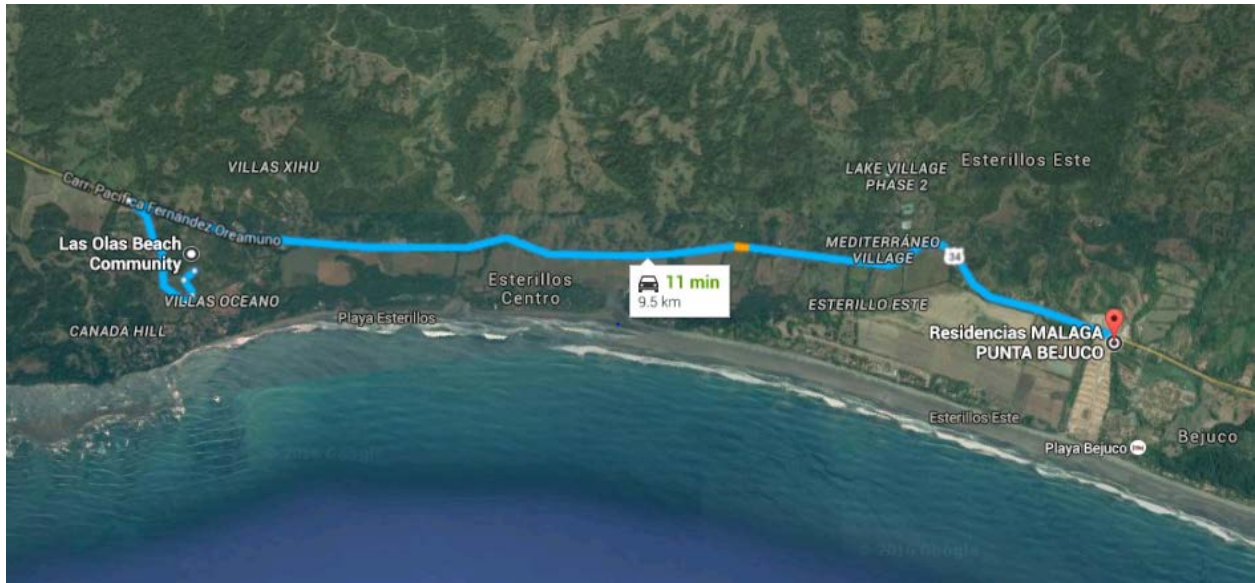
¹³⁵ See Google Maps Search: Las Olas Beach Community to Residencias Malaga, Punta Bejuco. (CLEX-115).

¹³⁶ See Malaga Residences Presentation (CLEX-058).

¹³⁷ See Malaga Residences Presentation (CLEX-058).

¹³⁸ See Malaga Residences Presentation, June 2016. (CLEX-120).

Figure IV Distance Between Las Olas and Malaga



Source: Google Maps Search – Las Olas to Residencias Malaga (CLEX-115).

II.3.2.a.iii Costa del Sol

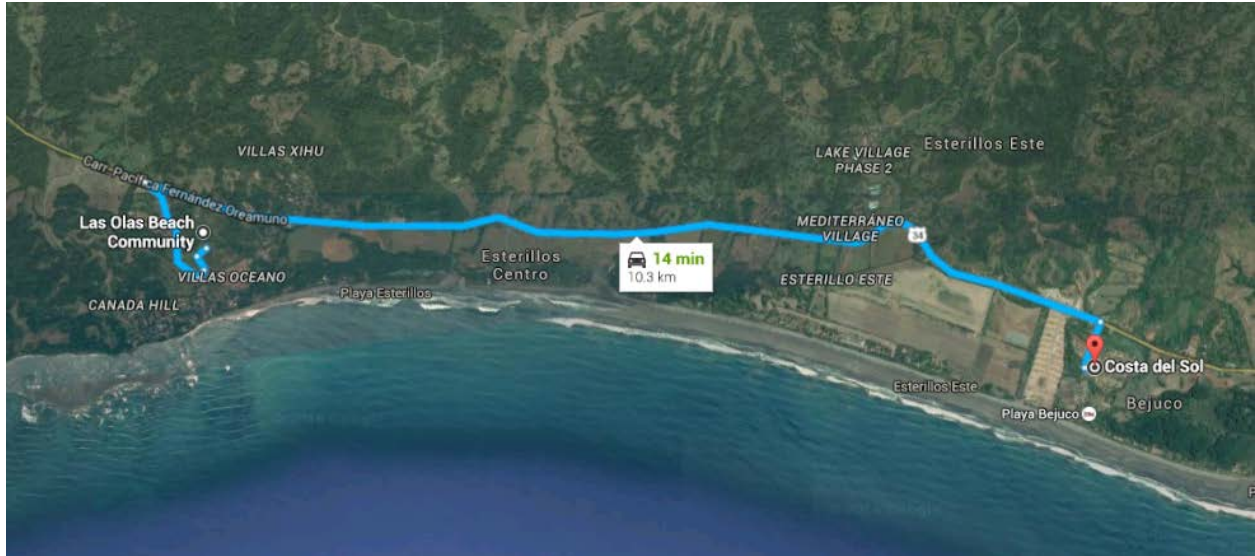
103. Costa Del Sol is a private resort style gated community located in Playa Bejuco, Puntarenas 10.3 km to the south of the Las Olas Project.¹³⁹ The gated community consists of 127 lots, all of which have been sold and are owned privately.¹⁴⁰ Out of the 127 lots, 71 of them have completed private residences. Thus, Costa Del Sol offers homes and lots available for resale, and homes are available for rent by the week or month.¹⁴¹

¹³⁹ See Google Maps Search: Distance from Las Olas Beach Community to Costa Del Sol (CLEX-116).

¹⁴⁰ See Costa Del Sol Neighborhood Association Website. Available at <http://www.costadelsolcostarica.com/en/>. (Last accessed July 22, 2016) (CLEX-117).

¹⁴¹ See Costa Del Sol Neighborhood Association Website. Available at <http://www.costadelsolcostarica.com/en/>. (Last accessed July 22, 2016) (CLEX-117).

Figure V Distance Between Las Olas and Costa del Sol



Source: Google Maps Search Las Olas to Costa del Sol (CLEX-116).

II.4 RESIDUAL VALUE OF LAND

104. In section 8.5 of his report, Mr. Hart argues that the methodology I use to estimate the residual value of the 39 hectares of Las Olas Project land after the Measures is “*overly simplistic*” and contains several flaws.¹⁴² Mr. Hart claims that the “*mistake*” that discredits my residual land valuation the most is that I do not make adjustments to the three listings I use from my REMAX source, making my valuation unreliable.¹⁴³

105. My methodology to calculate the residual value of the Las Olas Project land, however, is based on a broad search of market comparables.¹⁴⁴ I searched through 104 vacant lot listings to find properties comparable to the Las Olas Project site after the Measures.

¹⁴² See Hart Report, ¶165.

¹⁴³ See Hart Report, ¶ 166. See also Abdala First Report, Table 10. See also Remax Caribbean Islands Real Estate Listings site. Vacant Land For Sale in Puntarenas, Costa Rica. Available at <http://www.remaxcaribbeanislands.com> (Last accessed November 16, 2015). (CLEX-050).

¹⁴⁴ See Abdala First Report, section IV.4.3.

From the 104 Puntarenas listings, I determined the most comparable listings by applying three criteria.

- a. Minimum size requirement of 10 hectares;
- b. Must include forest or rainforest on the property;
- c. Those not described as “*ready to build*” or with any water/sewage connections;¹⁴⁵

106. From the 104 listings only three properties fit all of these criteria. Since my first report, I have expanded my search for more comparable land, but have not found any such properties. This is unsurprising given that there does not seem to be an established market in Costa Rica for land that is not suitable for construction, or developing real estate.¹⁴⁶ Therefore, in my updated model I keep on using a value for the residual land at a price of US\$ 1.36 per m² as of May 2011 adjusted by the transaction to listing price discount.¹⁴⁷

II.5 RESPONSES TO OTHER TOPICS RAISED BY MR. HART

II.5.1 A Cost-Base Approach as Proposed by Mr. Hart Does Not Measure Fair Market Value

107. Mr. Hart proposes the use of the cost approach based on historical costs incurred to assess the value of the Las Olas Project.¹⁴⁸ Even though he attempts to characterize this as an “asset-based cost approach” that could be used to determine the market value of an

¹⁴⁵ In my first report, I refer to this criteria as “*virgin land*.” See Abdala First Report, ¶127.

¹⁴⁶ See Abdala First Report, ¶127.

¹⁴⁷ See Abdala First Report, ¶128.

¹⁴⁸ See Hart Report, ¶182. Contrary to Mr. Hart’s allegation that Claimants have not put forward the necessary supporting details that would support a cost claim, the cost information was submitted in my model in the worksheet “*Past Invmt*” and supported by exhibits (CLEX-022) and (CLEX-004). See “*Past Invmt*” worksheet, CL Valuation Model (CLEX-003). See also Profit and Loss Statement Detail of Cotsco and Las Olas Capital, 2002-2011 (CLEX-022). See also Sale and Purchase Agreement of 2002 (CLEX-004).

asset, his proposed methodology, based on historically incurred cash costs spent by the investor, does not equate to the value of the asset under an cost-based or asset-based approach, it is not a generally accepted valuation methodology in financial literature, nor does it fit the definition of the cost approach provided by Mr. Hart himself.¹⁴⁹

108. Mr. Hart provides the right definition of the cost based approach: “*The cost approach is a general way of determining a value indication of an individual asset by quantifying the amount of money required to replace the future service capability of the asset.*”¹⁵⁰ He quotes this definition from the Litigation Services Handbook. Mr. Hart, however, claims that “*The cost approach measures the actual amount spent on the project to date and evaluates the contribution to value made by these funds. (...) [T]here is an assumption that the value of the property has a direct correlation to the funds spent.*”¹⁵¹ Whereas the financial definition determines the value of the asset based on a current market price of *replacement costs*, Mr. Hart misrepresents the methodology to base it on a historic account of incurred funds spent. The two concepts are very dissimilar as the current price of replacing an asset can be higher (or lower) than the funds actually spent to build it.

109. While the methodology definition provided by Mr. Hart is sound from a financial perspective and shared by financial authors, Mr. Hart’s application is nowhere to be found in financial literature. As Pratt explains in his book, the asset-based cost approach is based on the principle of substitution; “*no one would pay more for an asset than the price required to obtain (by purchase or construction) a substitute asset of comparable*

¹⁴⁹ See Hart Report, ¶62.

¹⁵⁰ See Hart Report, ¶73. Mr. Hart quotes this definition from the Glossary of the Litigation Service Handbook. See Weil, Roman L., Peter B. Frank, Christian W. Hughes, and Michael J. Wagner. 2007. *Litigation Services Handbook: The Role of the Financial Expert*, 4th Ed: John Wiley & Sons, Inc. p. 27 (CREG-13).

¹⁵¹ See Hart Report, ¶73.

*utility”.*¹⁵² As Pratt points out, however, the historic costs are very rarely an indicator of the substitution value, he says *“In fact, accounting book value is not a business valuation method at all (...) the values presented on the cost-based balance sheet are usually not representative of a current economic value for business valuation purpose.”*¹⁵³

110. Pratt also comments on the applicability of the methodology:

*“(...) the cost approach assumes that substitute properties of comparable utility may be obtained. If, in fact, the subject asset is unique in one or more respects, the cost approach may not be a viable valuation method.”*¹⁵⁴

111. Mr. Hart provides no support as to why this methodology could be applied to determine the fair market valuation of the Las Project and how such methodology would comply with a full compensation principle, from a damage valuation perspective.

¹⁵² See Pratt, Shannon P., and Alina V. Niculita. 2008. *Valuing a Business, The Analysis and Appraisal of Closely Held Companies*, 5th Ed. New York: McGraw Hill. p. 358 (CLEX-093).

¹⁵³ See Pratt, Shannon P., and Alina V. Niculita. 2008. *Valuing a Business, The Analysis and Appraisal of Closely Held Companies*, 5th Ed. New York: McGraw Hill. p. 352 (CLEX-093).

¹⁵⁴ See Pratt, Shannon P., and Alina V. Niculita. 2008. *Valuing a Business, The Analysis and Appraisal of Closely Held Companies*, 5th Ed. New York: McGraw Hill. p. 358 (CLEX-093).

III. VALUATION ADJUSTMENTS AND UPDATE

III.1 ADJUSTMENTS TO PARAMETERS TO THE GOING CONCERN VALUATION

112. I expanded the research of parameters for my valuation exercise of Las Olas as a going concern and as a result I make some adjustments based on the additional market information I found. I also make some corrections which I deem appropriate, based on some of the observations raised in Mr. Hart's First Report.

III.1.1 Revenues

III.1.1.a Discount of Sales Prices to Listing Prices

113. In my original model, to recognize that listed prices are usually higher than actual transaction prices, I reduced listed prices by an average 10% discount, which I found to be reasonable based on the general workings of asset valuation in the real estate industry, and given that such statistical data is not available for the Costa Rican market.¹⁵⁵

114. For this report I have expanded my research and found more precise information on the relationship between listing prices and actual selling prices in 2015, as reported by Coldwell Banker's Florida Keys Real Estate Market Comparison Report. This information, even though it is based on the U.S. market provides a valuable insight as to the ratio of listing/selling prices in a location that is also used as beach resort destination and is contemporaneous to the time for which I collected primary listing price information from Costa Rica.¹⁵⁶

¹⁵⁵ See Abdala First Report, ¶89. See also "Parameters" Worksheet, cell (F24) CL Valuation Model (CLEX-003). See also Hart Report, ¶¶ 7 (ii-iv), 113 footnote 37. 118 (ii), 125, 165, criticizing the use of a 10% discount to listing prices.

¹⁵⁶ See Coldwell Banker, "Florida Keys Real Estate Market Comparison: January – December 2015 vs. 2014." p.1 Available at <http://www.realestatefloridakeys.com/files/141/Winter2016ResidentialRENNewsletter.pdf>. (Last accessed June 15, 2016) (CLEX-118).

115. The report finds that in the Florida Keys real estate market in 2015, the average “*Sales Price to Original List Price*” ratio was 89.99%, and the average “*Sales Price to Final List Price*” ratio was 94.39%.¹⁵⁷ This means that selling prices in the Florida Keys were transacted at a 5.6% discount in relation to their latest listing price and at a 10.0% discount in relation to their original listing price. This reveals a common pattern in the industry, in which properties that are harder to sell tend to reduce their listing prices over time. The data that I collected on listing prices in Costa Rica, however, does not allow me to distinguish whether the observed listing price is the “original” one or the “latest” before a transaction is accomplished. Because the sample would contain both properties that have been listed for the first time as well as properties that have been already listed for some time and for which downward price adjustments have already been made, I assume that the size of the discount that the sample comprises would be an average of both discounts (5.6% and 10.0%), which provides an overall discount on listed prices of 7.81%.¹⁵⁸

116. As a consequence, I have updated the discount that is applied to my model to derive selling prices for lots, houses, and condos, from 10.0% to 7.8%. The stand-alone effect of this update is an increase of the valuation for the Las Olas Project as a going concern by 3.2% as of May 2011, from US\$ 93.1 million to US\$ 96.1 million.

III.1.1.b Lots' Size

117. In my original report I estimate the size of lots based on the configuration of the December 2010 Business Plan.¹⁵⁹ In this business plan, Las Olas management states that

¹⁵⁷ Coldwell Banker, “Florida Keys Real Estate Market Comparison: January – December 2015 vs. 2014”. p.1 Available at <http://www.realestatefloridakeys.com/files/141/Winter2016ResidentialRENNewsletter.pdf>. (Last accessed June 15, 2016) (CLEX-118).

¹⁵⁸ See “Parameters” Worksheet, CL Valuation Model – Second Report (CLEX-082).

¹⁵⁹ See Abdala First Report, ¶83.

“the lots will be between 500 and 700 square meters.”¹⁶⁰ In my model I use the average of this range (at 600m²) as the representative lot size for the project.

118. To provide more precision to this estimate, I now calculate the average lot size for Las Olas based on the lot configurations of the Master Site Plan.¹⁶¹ The computations from this site plan indicate that the precise average lot size according to Master Site Plan is slightly larger, at 649 m².¹⁶²

119. Adjusting the lot size, as a stand-alone basis, increases the valuation of Las Olas as going concern as of May 2011 by 0.26% from US\$ 93.1 million to US\$ 93.3 million.¹⁶³

III.1.1.c Lots Comparable Prices

120. When computing the comparable prices for lots there was a data entry error related to the price of Property 2 (“Calle Hermosa”). Rather than US\$ 39,000¹⁶⁴, the correct value was US\$ 35,000.¹⁶⁵ The effect of adjusting this in my valuation of the project as a going concern as of May 2011 is a reduction of less than 0.01%.

III.1.1.d Houses' Comparable Prices

121. In my original report, I use the Malaga residences as one of the sources to estimate comparable house selling prices.¹⁶⁶ When estimating the average selling price per m² for these residences, however, I used the maximum and the minimum price per house type rather than the mid-range observations. I now recalculate the average price for the

¹⁶⁰ See Las Olas Business Plan, December 2010. p. 11 (CLEX-016).

¹⁶¹ See Master Site Plan, September 2008. (CLEX-015).

¹⁶² See “Average Lot Size Calculation” worksheet, CL Valuation Model – Second Report. (CLEX-082).

¹⁶³ See Hart Report, ¶111 footnote 32, on his comments to the average lot size.

¹⁶⁴ See Remax Caribbean Islands Real Estate Listings site. Vacant Land for Sale in Puntarenas, Costa Rica. Available at <http://www.remaxcaribbeanislands.com>. (Last Accessed November 16, 2015). p. 1 (CLEX-050).

¹⁶⁵ See Remax Caribbean Islands Real Estate Listings site. Vacant Land for Sale in Puntarenas, Costa Rica, Available at <http://www.remaxcaribbeanislands.com>. (Last Accessed November 16, 2015). p. 1 (CLEX-050). See also Hart Report, ¶111 footnote 33, on his comments to the comparable prices of lots.

¹⁶⁶ See Malaga Residences Presentation (CLEX-058).

Malaga properties including all the mid-range observations per house type rather than only the maximum and minimum ones, as their inclusion allows for the use of larger and richer information. Table III shows per type of residence the average price per square meter as originally calculated compared with this adjustment.

Table III Malaga Average Prices per m²

Name of Property	Average US\$ Price per m ²		
	Original	Adjusted	% Difference
Modelo Cielo	1,926	1,870	-2.9%
Modelo Malaga	1,809	1,763	-2.5%
Modelo Malaga Rock	1,733	1,694	-2.2%
Malaga Average Price	1,823	1,776	-2.6%

Source: Own production based on pricing from Malaga Residences Presentation (CLEX-058).

122. The stand-alone effect of incorporating this adjustment on Málaga average prices into my model is a 0.5% decrease in the valuation of the project as a going concern as of May 2011, from US\$ 93.1 million to US\$ 92.6 million.¹⁶⁷

III.1.1.e Homeowners' Association (HOA) Revenues

123. In my original model, I did not include Homeowners' Association (HOA) revenues in the houses and condominiums segment, but rather only for timeshares.¹⁶⁸ However, in my current research I find that these kind of communities usually charge HOA fees in exchange of maintenance services. I have therefore added HOA fees, net of costs to both houses and condominiums using the same methodology used to calculate the maintenance fees of timeshares.

¹⁶⁷ See Hart Report, ¶ 123, on his observations to the averaging of Malaga selling prices.

¹⁶⁸ See Abdala First Report, ¶112 footnote 114.

124. In my adjusted model, based on comparable developments, I assume that HOA fees would be US\$150 per month per house or condo.¹⁶⁹ Based on this, my adjusted model calculates the added revenue using the same methodology for the timeshares segment, that is, a markup on costs of 12.5%.¹⁷⁰ Including the revenues from HOA fees my valuation for the Las Olas Project as a going concern as of May 2011 increases by 0.9% from US\$ 93.1 million to US\$ 93.9 million.

III.1.1.f Timeshare Prices and Maintenance Fees

125. In my initial research I found information on timeshare interval pricing and maintenance fees for the United States, which I used in my first report.¹⁷¹ As I expanded my research in the preparation of this report I found timeshare pricing and maintenance fee information for Costa Rica reported by Resort Condominiums International's (RCI) for 2011 through 2014.¹⁷²

126. I update my model to include these timeshare interval prices and maintenance fees for Costa Rica, which are more suitable to the valuation of Las Olas timeshare business segment. Table IV below compares the interval prices and maintenance fees from my original model with the updated. As the table shows, the updated interval prices for Costa Rica are lower, whereas the maintenance fees are lower for 2011 and 2012, almost identical for 2013, and higher for 2014.

¹⁶⁹ See HOA Fees Email from El Mistico Sales Representative, July 21, 2016 (CLEX-122).

¹⁷⁰ See Abdala First Report, ¶112 footnote 114.

¹⁷¹ See Abdala First Report, ¶107.

¹⁷² See RCI, *Latin America and the Caribbean Vacation Ownership Factbook*, Mexico D.F, Mexico, 2011. pp. 40-47 (CLEX-086). See also RCI, *Latin America and the Caribbean Vacation Ownership Factbook*, Mexico D.F, Mexico, 2012. pp. 24-28 (CLEX-087). See also RCI, *Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean* Mexico D.F, Mexico, 2013. pp. 24-29 (CLEX-088). See also RCI, *Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean*, Mexico D.F, Mexico, 2014. pp. 33-37 (CLEX-089).

Table IV Time Share Price per Interval and Maintenance Fees 2011-2014

	2011	2012	2013	2014
Interval Prices (US\$ per Week)				
Original	16,711	17,062	17,420	17,786
Adjusted	12,398	11,086	12,588	12,261
Maintenance Fees (US\$ per Week)				
Original	762	778	794	811
Adjusted	487	695	793	840

Source: Own Production - Original values from “Segments” Worksheet CL Valuation Model (CLEX-003). Adjusted values from “RCI Timeshare Data” Worksheet, CL Valuation Model – Second Report (CLEX-082).

127. Introducing this adjustment on timeshare pricing and maintenance fees to my model results in a stand-alone reduction of my valuation of the Las Olas project as a going concern as of May 2011 of 7.9%, from US\$ 93.1 million to US\$ 85.8 million.¹⁷³

III.1.1.g Timeshare Financing Terms

128. The RCI Central America Fact Books also provide timeshare financing data for Costa Rica.¹⁷⁴ Specifically, RCI reports the average size of the down payment (*i.e.*, the portion of the purchase price that is self-financed by the buyer) and the average interest rate charged by developers for sales of Costa Rican timeshares from 2011 through 2014.

¹⁷³ See Hart Report, ¶¶ 128, 134 on his observations to timeshare pricing. Mr. Hart wonders why the model uses a 14% discount on listing prices for timeshares units, whereas such discount is 10% on lots, houses, and condos. The 14% parameter for timeshares units comes directly from a primary source for my timeshare estimates, the JMP Report. Looking at the timeshare industry as a whole, the report states that “86% of existing intervals are owned by timeshare owners, 12% are still unsold and owned by developers, and 2% are owned by HOAs. [Home Owner’s Association]” See JMP Report, JMP Securities, “Lodging: Timeshare Demystified – JMP’s Investor Guide to the Vacation Ownership Business,” January 23, 2014, p. 9 (CLEX-067). See also Hart Report, ¶134.

¹⁷⁴ See RCI, *Latin America and the Caribbean Vacation Ownership Factbook*, Mexico D.F, Mexico, 2011. p. 45 (CLEX-086). See also RCI, *Latin America and the Caribbean Vacation Ownership Factbook*, Mexico D.F, Mexico, 2012. p. 28 (CLEX-087). See also RCI, *Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean* Mexico D.F, Mexico, 2013. p. 28 (CLEX-088). See also RCI, *Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean*, Mexico D.F, Mexico, 2014. p. 36 (CLEX-089).

129. My original model estimated the average down payment for timeshares at 15%, whereas the RCI reports for Costa Rica indicate that the size of down payment is higher, up to 30%. I have updated this figure accordingly, to reflect new information that is closer and thus more suitable to the target asset. As it relates to the average interest rate, my model used 16.9% for the timeshares segment based on my research on the U.S. timeshare industry from the JMP Securities Report.¹⁷⁵ The RCI reports for Costa Rica show interest rates ranging at very similar values, from 16.8% in 2011 to 18.7% in 2014. I now adjust interest rates with the information from the RCI reports.¹⁷⁶
130. Lastly, the RCI reports also estimate that the average cancellation of the loans is of five years for Costa Rica, instead of the 10 years that I have assumed, based on the evidence from the US market.¹⁷⁷ I also adjust my model to reflect this new information.
131. Based on this information I adjust the model so that now it uses the average timeshare down payment of 30%, a loan time repayment of 5 years, and interest rates for the historical period ranging from 16.8% to 18.7%.

¹⁷⁵ See JMP Report, JMP Securities, “Lodging: Timeshare Demystified – JMP’s Investor Guide to the Vacation Ownership Business,” January 23, 2014, p. 13 (CLEX-067).

¹⁷⁶ After 2014, my updated model uses the last interest rate available at 18.7%. See “VOI Evolution” Worksheet, Row 11, CL Valuation Model – Second Report (CLEX-082). See also RCI, *Latin America and the Caribbean Vacation Ownership Factbook*, Mexico D.F, Mexico, 2011. p. 45 (CLEX-086). See also RCI, *Latin America and the Caribbean Vacation Ownership Factbook*, Mexico D.F, Mexico, 2012. p. 28 (CLEX-087). See also RCI, *Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean* Mexico D.F, Mexico, 2013. p. 28 (CLEX-088). See also RCI, *Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean*, Mexico D.F, Mexico, 2014. p. 36 (CLEX-089). See Hart Report, ¶¶ 7 (v), 128, on Mr. Hart’s comments to timeshare cash flows assumptions.

¹⁷⁷ See Morgan Stanley Report, “Timeshare 101,” March 30, 2015. p. 12 (CLEX-066). See also RCI, *Latin America and the Caribbean Vacation Ownership Factbook*, Mexico D.F, Mexico, 2011. p. 45 (CLEX-086). See also RCI, *Latin America and the Caribbean Vacation Ownership Factbook*, Mexico D.F, Mexico, 2012. p. 28 (CLEX-087). See also RCI, *Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean* Mexico D.F, Mexico, 2013. p. 28 (CLEX-088). See also RCI, *Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean*, Mexico D.F, Mexico, 2014. p. 36 (CLEX-089).

132. The combined stand-alone effect of these three adjustments to timeshare financing parameters on my valuation for the Las Olas Project as a going concern as May 2011 is a decrease of 2.4%, from US\$ 93.1 million to US\$ 90.8 million.

III.1.2 Costs

III.1.2.a Houses Construction Time

133. Based on my initial research of house construction time estimates from the Wall Street Journal article; “Average Time to Build a House: 6 months”¹⁷⁸, my original model and report approximated that the average construction time for new homes at the Las Olas Resort would be six months.¹⁷⁹

134. I have now updated my model to account for the potential delays in construction time that may result in a longer construction period. I base my increased estimates on two sources cited in my original report; a Costa Rican article on building permits and timelines,¹⁸⁰ and another local article on the building process in Costa Rica¹⁸¹. The first Costa Rican article estimates that the building of an averaged sized house should take “between 6 and 10 months”¹⁸², whereas the other local article provides estimates for each stage of the building process in Costa Rica, and approximates time lengths of 6.5 weeks for “Property Research & First Draft,” 6.5 weeks for “Construction Plans,” 9 weeks for “Building Permits, and 33 weeks for “Construction.”¹⁸³ Thus, according to the latter the total building process in Costa Rica averages 55 weeks, or approximately 1 year, while

¹⁷⁸ See The Wall Street Journal, “Average Time to Build a House: 6 Months” January 7, 2015. (CLEX-055).

¹⁷⁹ Mr. Hart pointed out that my original 6-month construction time was inconsistent with other sources cited. See Hart Report, ¶119 (i).

¹⁸⁰ See Costa Rica Real Estate Site. Permits, Costs and Timelines. Available at <http://costarica-information.com/about-costa-rica/economy/economic-sectors-industries/real-estate/real-estate-general/construction/permitscosts-timelines> (Last accessed November 24, 2015) (CLEX-056).

¹⁸¹ See Costa Rica Real Estate Guide. Building Process Page. Available at <http://costarica.com/real-estate/building-process/> (Last accessed November 23, 2015) (CLEX-060).

¹⁸² See Costa Rica Real Estate Site. Permits, Costs and Timelines. p. 2 (CLEX-056).

¹⁸³ See Costa Rica Real Estate Guide. Building Process Page, p.2 (CLEX-060).

construction time alone only accounts for 33 weeks (which is the equivalent to 7.6 months).

135. I have adjusted my model, to account for a total construction time of 7.6 months, rather than 6 months as I had originally considered. The stand-alone effect of this adjustment on my valuation for the Las Olas Project as a going concern as of May 2011 decreases by 0.2%, from US\$ 93.1 million to US\$ 92.9 million.

III.1.2.b Timeshare Sales General & Administrative Expenses

136. In my original model I calculated the sales marketing cost component for the Las Olas timeshares segment as 42% of total sales.¹⁸⁴ This estimate was an average based on evidence from the U.S., contained in a Merrill Lynch Report that found timeshare marketing costs to range between 36% and 47%.¹⁸⁵

137. In my update I expand the evidence available for marketing and general and administrative costs to include the three sources I cite in my original report for timeshares (JMP Report, Merrill Lynch, and Morgan Stanley).¹⁸⁶ My updated model therefore calculates a total sales general & administrative expense by taking the average of the total sales marketing cost and general & administrative expense (as a % of net sales) from the JMP Report, the Merrill Lynch Report, and the Morgan Stanley Report.

¹⁸⁴ See Abdala First Report, ¶ 109.

¹⁸⁵ See Merrill Lynch Report, "Timeshare is a Small, Secular Growth Story." September 19, 2007, p. 3 (CLEX-068).

¹⁸⁶ Mr. Hart criticized my use of the 42% marketing as a percentage of sales estimate from the Merrill Lynch Report, arguing that it was lower than the range reported by JMP Securities, at 45% to 65%. See Hart Report, ¶ 129. See also Merrill Lynch Report, "Timeshare is a Small, Secular Growth Story." September 19, 2007, p. 3 (CLEX-068). See also JMP Report, JMP Securities, "Lodging: Timeshare Demystified – JMP's Investor Guide to the Vacation Ownership Business," January 23, 2014, p. 11. (CLEX-067). See also Morgan Stanley Report, "Timeshare 101," March 30, 2015, p. 20. (CLEX-066).

Table V Total Timeshare Sales General & Administrative Expense

	JMP Report		Merrill Lynch		Morgan Stanley	Average
	Min	Max	Min	Max		
Marketing Cost (% of Sales)	45%	65%	36%	47%	41%	
G&A Costs (% of Sales)					8%	
Total (SG&A)	45%	65%	36%	47%	49%	48%

Source: Own Production - Merrill Lynch Report, “Timeshare is a Small, Secular Growth Story.” p. 3 (CLEX-068). JMP Report, JMP Securities, “Lodging: Timeshare Demystified – JMP’s Investor Guide to the Vacation Ownership Business” p. 11 (CLEX-067), Morgan Stanley Report, “Timeshare 101” March 30, 2015, p. 20. (CLEX-066)

138. My updated model has an average total marketing, general & administrative expense of 48%, representing a net increase of 6% with respect to my original report.¹⁸⁷ When I apply this adjustment to my model, the stand-alone effect on my valuation for the Las Olas Project as a going concern as of May 2011 results in a decrease by 2.5%, from US\$ 93.1 million to US\$ 90.8 million.

III.2 UPDATES TO LAND APPRAISAL

139. The appraisal prepared by Mr. Calderon (on which I have based the land value scenario) only includes the appraisal of one of the 72 lots that comprise the roadside lots area highlighted in Figure VI below:

¹⁸⁷ As a result of this adjustment, my adjusted model’s profit margin ranges from 36% in 2011 to 31% in 2015, down from 46% and 43% respectively in my original model. The adjusted profit margins are still higher than those reported in the U.S. benchmarks cited in the JMP Report, the Merrill Lynch Report and those implicit in the Morgan Stanley report (ranging from 17% to 32%), most likely reflecting the lower labor and construction costs in Costa Rica, as compared to the U.S. market. See Merrill Lynch Report, “Timeshare is a Small, Secular Growth Story.” September 19, 2007, p. 3 (CLEX-068). See also JMP Report, JMP Securities, “Lodging: Timeshare Demystified – JMP’s Investor Guide to the Vacation Ownership Business,” January 23, 2014, p. 11 (CLEX-067). See also Morgan Stanley Report, “Timeshare 101,” March 30, 2015, p. 20 (CLEX-066). See also Hart Report, ¶130 on his observations to timeshares profit margins.

Figure VI Roadside Lots



Source: Master Site Plan, September 2008 (CLEX-015)

140. To compute the value of this whole area, in my original report I multiplied the value of the appraised lot by the total number of lots (72).¹⁸⁸ To add more precision to my calculation, however, in the update I estimate the total surface of this area and multiply it by the value per square meter from Mr. Calderon's appraisal of the lot by the total surface of the area, which I obtain by adding the square meters for each lot as shown in Figure VI above.¹⁸⁹

141. Introducing this adjustment in the land appraisal reduces the valuation of land in its current state as of May 2011 and November 2015 by 0.8%, on a stand-alone basis, from US\$ 35.5 million to US\$ 35.2 million.

III.3 ADJUSTED VALUATION RESULTS

III.3.1 Going Concern

142. In Table VI, I summarize the adjusted valuation of the project as a going concern as of May 2011 compared to my original valuation. Due to the adjustments described above, my adjusted valuation is 7.6% lower than my original May 2011 valuation, decreasing from US\$ 93.1 million to US\$ 86.0 million.

¹⁸⁸ See Abdala First Report, ¶124. See also Hart Report, ¶158.

¹⁸⁹ To calculate the total surface area of the 72 roadside lots, I rely on the September 2008 Master Site Plan for the Las Olas Project. See Figure VI. The plan includes the area dimensions (m²) for each of the 72 lots, which I summed to arrive at the total surface area. See Master Site Plan, September 2008 (CLEX-015).

Table VI Value of Las Olas as a Going Concern as of May 2011

US\$ Million of May 2011		
	Original	Adjusted
Value of Going Concern	93.1	86.0
PV of FCFF		
<i>Lots</i>	15.5	17.8
<i>Houses</i>	22.2	21.8
<i>Condos</i>	24.4	25.6
<i>Timeshares</i>	23.5	13.0
<i>Hotel</i>	7.6	7.9

Source: CL Valuation Model – Second Report (CLEX-082)

III.3.2 Land Value

143. In Table VII, I compare my original valuation of the land as of May 2011 with the adjusted valuation as of the same date. The adjusted May 2011 land appraisal is 0.8 % lower than in my original assessment, decreasing from US\$ 35.5 million to US\$ 35.2 million.

Table VII Las Olas Property But-For Land Value as of May 2011

US\$ Million as of May 2011		Unit	Original	Updated
Total Land Value	[a]	2009 MM Col.	9,658	9,533
Total Urbanization Value	[b]	2009 MM Col.	20,447	20,447
Progress of Project	[c]	%	33%	33%
Las Olas Urbanization Value	[d]=[b]*[c]	2009 MM Col.	6,704	6,704
2009 Appraisal in Current State	[e]=[a]+[d]	2009 MM Col.	16,362	16,237
Inflation Index	[f]		1.08	1.08
Exchange Rate	[g]	Col./US\$	500	500
Land Appraisal	[h]=[e]*[f]/[g]	MM US\$	35.5	35.2

Source: CL Valuation Model – Second Report (CLEX-082)

III.3.3 Summary of Damages to Claimants' Investments in Las Olas as of May 2011

144. Table VIII compares my original valuation of damages to Claimants on its investments in the Las Olas Project as of May 2011 with my updated valuation as of the same date. The updated May 2011 valuation of Damages is 6.6% lower than my original assessment, decreasing from US\$ 74.0 million to US\$ 69.1 million.

Table VIII Damages to Claimants' Investments in Las Olas as of May 2011

US\$ Million of May 2011		
	Original	Updated
(+) But-For Expected Value	74.4	69.6
Value of Going Concern (68%)	93.1	86.0
PV of FCFF		
<i>Lots</i>	15.5	17.8
<i>Houses</i>	22.2	21.8
<i>Condos</i>	24.4	25.6
<i>Timeshares</i>	23.5	13.0
<i>Hotel</i>	7.6	7.9
Value of Land (32%)	35.5	35.2
(-) Actual Value	0.4	0.5
Damages to Claimants as of May 2011	74.0	69.1

Source: CL Valuation Model – Second Report (CLEX-082)

III.4 UPDATE OF NEW PARAMETERS FOR THE 2016 DATE OF VALUATION

145. As instructed by Counsel to Claimant, I undertake the valuation of damages as of two dates, the effective date of the Measures (May 12, 2011) and a current date (November 30, 2015). As explained in my first report, the latter needs to be updated in each stage of this procedure to reflect changes in the market conditions and the date to which cash flows are discounted (compounded).¹⁹⁰ In order to do so, I have made the following updates to my current date valuation:

¹⁹⁰ See Abdala First Report, ¶52 and footnote 62.

- a. I update my forecast for US inflation. Based on the most current Federal Reserve Bank of Philadelphia Survey of Forecasters of May 2016, the forecasted inflation for 2016-2025 is 2.2%, slightly higher than the forecast as of November 2015 of 2.1%.¹⁹¹
- b. I update my discount rate from 8.01% to 8.76% using the most current information available.¹⁹²
- c. I look at the real estate market conditions in Costa Rica and their evolution in the last eight months, since my first report. I find that there have been only minor movements in the overall listing prices of real estate property in the Costa Rican market.¹⁹³
- d. I modify the date of valuation as of a current date from November 2015 to July 2016. This affects the amount of periods cash flows are discounted or carryforward. In my updated valuation, cash flows prior to July 2016 will be carried forward to July 2016 and cash flows expected after that date are discounted to July 2016.
- e. In the case of the value of land in the but-for scenario, I use Mr. Calderón's appraisal as a basis and update it to the more current July 31, 2016 date of valuation, using the same indexation methodology as used in my First Report.¹⁹⁴
- f. To update the value of the actual scenario, I use the same indexation methodology as I do to the value of land in the but-for scenario.

¹⁹¹ See Federal Reserve Bank of Philadelphia. Second Quarter 2016 Survey of Professional Forecasters. May 13, 2016. **(CLEX-112)**.

¹⁹² See Appendix B for a description of the WACC update.

¹⁹³ For example, if I had updated the information on prices per m² for the comparable developments El Mistico and Malaga the resulting prices per m² would not have changed substantially. As it relates to lots, the average lot listing price/m² of first and second stage lots at El Mistico increased by 5%. When it comes to houses, the average house listing price/m² at Malaga increased by 19% but decreased in El Mistico by 16% resulting in an overall average increase on the price per m² for houses of only 2%. Lastly, the average price of apartments at El Mistico remained unchanged. See Email from El Mistico Sales Representatives, dated November 4, 2015 **(CLEX-051)**. See also Email from El Mistico Sales Representative, dated June 02, 2016 **(CLEX-121)**. See also El Mistico Presentation, June 2016. Available at <http://online.fliphtml5.com/kdct/gnkp/#p=1>. (Last accessed June 25, 2016) **(CLEX-119)**. See also Malaga Residences Presentation **(CLEX-058)**. See also Malaga Residences Presentation, June 2016 **(CLEX-120)**.

¹⁹⁴ See Abdala First Report, ¶122.

III.4.1 Updated Damage Results for a “Most Current” Date of Valuation Exercise

146. Table IX compares the valuation as of November 2015 with the valuation as of a most current date, July 2016, after introducing the aforementioned updates as well as the adjustments explained in section III.1. Overall, damages to Claimants decrease by 4.3% from US\$ 96.2 million as of November 2015 to US\$ 92.0 million as of July 2016.

**Table IX Updated Damages at a Most Current Date of Valuation:
July 2016 compared to November 2015**

US\$ Million		
	US\$ Million of Nov 2015	US\$ Million of July 2016
(+) But-For Expected Value	96.7	92.5
Value of Going Concern (68%)	124.1	118.1
PV of FCFF		
<i>Lots</i>	21.4	26.3
<i>Houses</i>	28.6	27.7
<i>Condos</i>	31.9	34.0
<i>Timeshares</i>	31.5	18.2
<i>Hotel</i>	10.6	11.9
Value of Land (32%)	39.4	39.2
(-) Actual Value	0.5	0.5
Damages to Claimants as of DoV	96.2	92.0

Source: CL Valuation Model – Second Report (CLEX-082)

III.5 PREJUDGMENT INTEREST

147. For the valuation as of the effective date of the Measures (May 2011), I have recommended to use the WACC as prejudgment interest, to be accrued on an annual

compounding basis, from the date of valuation until a current date, in this report July 2016.¹⁹⁵

148. In my original report I explained that the WACC (at 7.6%, computed as of 2011) or opportunity cost of capital, represents the annual return that the Las Olas Project would have earned, on average, had it been able to be launched as an ongoing business, and thus can be seen as the minimum compensation that the Project would have voluntarily accepted for the time delay on distributing its cash flows.

149. In this report I also propose two alternatives:

- a. First, I propose to use an interest rate based the cost of borrowing of the private sector in Costa Rica, based on the interest rate published by Costa Rican Central Bank on commercial loans made in US Dollars, which would have resulted in an average interest rate of 10% for the May 2011-July 2016 period. See Table X.
- b. Second, recognizing that the Las Olas Project might have not been completed, I construct an expected value index giving a 32% weight to the annual rate at which the land would expect to increase (in US dollar terms) during this period and a 68% weight to the opportunity cost of doing business. The opportunity cost of keeping the land in its current state is its appreciation in value, which in my valuation exercise is driven by the evolution of local inflation and the exchange rate. The resulting prejudgment interest rate would be equivalent to 6.8% per year during the relevant period.¹⁹⁶ See Table X, which offers a comparison of the overall cumulative impact on the prejudgment interest factor among these three alternatives.¹⁹⁷

¹⁹⁵ See Abdala First Report, Section IV.4.5.

¹⁹⁶ Note that in this calculation the compound factor will depend of the value of the asset in each scenario.

¹⁹⁷ See Central Bank of Costa Rica, Interest Rate on Commercial Loans, 2011 – May 31, 2016. Available at <http://indicadoreseconomicos.bccr.fi.cr/indicadoreseconomicos/Cuadros/frmVerCatCuadro.aspx?idioma=1&CodCuadro=613> (Last accessed May 31, 2016). (CLEX-090).

150. The second alternative that combines the WACC and the land appraisal index is the one rate that provides the best solution for this case, as it is the one that better resembles the characteristic of the target asset.

Table X Alternative PJI Rates Compared (2011-2016)

	May 2011- Dec 2011	Jan 2012- Dec 2012	Jan 2013- Dec 2013	Jan 2014- Dec 2014	Jan 2015- Dec 2015	Jan 2016- Jul 2016	May 2011- July 2016
PJI Based on WACC (original report)							
2011 WACC Rate	7.6%	7.6%	7.6%	7.6%	7.6%	7.6%	7.6%
WACC Index	1.05	1.08	1.08	1.08	1.08	1.04	1.47
PJI Based on Commercial Loan Rate							
Average Lending Rate	9.7%	10.9%	10.8%	10.1%	9.6%	9.7%	10.1%
Loan Rate Index	1.06	1.11	1.11	1.10	1.10	1.06	1.66
PJI Based on combined WACC and Land Appraisal Index							
Land Appraisal Rate	3.2%	5.6%	4.5%	-1.9%	-0.3%	-0.1%	2.1%
Land App Index	1.03	1.06	1.04	0.98	1.00	1.00	1.11
2011 WACC Rate	7.6%	7.6%	7.6%	7.6%	7.6%	7.6%	7.6%
WACC Index	1.05	1.08	1.08	1.08	1.08	1.04	1.47
Combined WACC and Land Appraisal Rate							6.8%
Combined WACC and Land Appraisal Index							1.41

Source: CL Valuation Model - Second Report (CLEX-082)

151. In Table XI I show the damage calculation as of the date of the measures updated to a current date (July 2016) using the alternative prejudgment rates.

Table XI Damage to Claimants as of May 2011, Updated to Current Date at Different Pre-Judgment Interest Rates

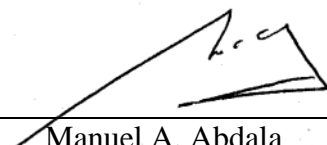
US\$ Million			
	Combined Land and WACC	WACC	Average Lending Rate
Damages to Claimants as of May 2011	69.1	69.1	69.1
<i>Average Pre-Judgement Rate</i>	<i>6.8%</i>	<i>7.6%</i>	<i>10.1%</i>
Pre-Judgement Interest	28.3	32.3	45.4
Damages to Claimants as of July 2016	97.4	101.4	114.5

Source: CL Valuation Model - Second Report (CLEX-082)

IV. DECLARATION

152. I declare that:

- a. I understand that my duty in giving evidence in this arbitration is to assist the arbitral tribunal decide the issues in respect of which expert evidence is adduced. I have complied with, and will continue to comply with, that duty;
- b. I confirm that this is my own, impartial, objective, unbiased opinion which has not been influenced by the pressures of the dispute resolution process or by any party to the arbitration;
- c. I confirm that all matters upon which I have expressed an opinion are within my area of expertise;
- d. I confirm that I have referred to all matters which I regard as relevant to the opinions I have expressed and have drawn to the attention of the arbitral tribunal all matters, of which I am aware, which might adversely affect my opinion;
- e. I confirm that, at the time of providing this written opinion, I consider it to be complete and accurate and constitute my true, professional opinion.



Manuel A. Abdala
August 4, 2016

1101 K Street NW – Suite 800
Washington, DC – 20005, USA

APPENDIX A LIST OF DOCUMENTS

Exhibit #	Description
82	CL Valuation Model Second Report
83	CL WACC Model Second Report
84	Koller, Tim, Marc Goedhart, and David Wessels. 2010. <i>Valuation: Measuring and Managing the Value of Companies</i> , 5 th Ed. New York: John Wiley & Sons.
85	RCI Timeshares Overview Webpage, Available at: http://www.rci.com/pre-rci-en_US/explore-rci/about-rci/overview/rci-overview.page
86	RCI, 2011. <i>Latin America and the Caribbean Vacation Ownership Factbook</i>
87	RCI, 2012. <i>Latin America and the Caribbean Vacation Ownership Factbook</i> ,
88	RCI, 2013. <i>Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean</i>
89	RCI, 2014. <i>Analysis and Perspectives of Vacation Ownership in Latin America and the Caribbean</i>
90	Central Bank of Costa Rica, Interest Rate on Commerical Loans, 2011 – May 31, 2016
91	Damodaran, Aswath, “Probalistic Approaches: Scenario Analysis, Decision Trees and Simulations,” Stern School of Business, New York University, 2008
92	Titman, Sheridan, and John D Martin. 2011. <i>Valuation: The Art and Science of Corporate Investment Decisions</i> , 2 nd Ed. Prentice Hall
93	Pratt, Shannon P., and Alina V. Niculita. 2008. <i>Valuing a Business, The Analysis and Appraisal of Closely Held Companies</i> , 5th Ed. New York: McGraw Hill
94	National Association of Realtors. Investment and Vacation Home Buyers Survey 2013
95	Fama, Eugene F., and Kenneth R. French. 1998. “Value versus growth: The international evidence,” <i>Journal of Finance</i> . 53 (6): 1975-1999

Exhibit #	Description
96	Barry, C. Goldreyer, E., Lockwood, L., and M. Rodriguez. 2001. "Robustness of Size and Value Effects in Emerging Equity Markets, 1985-2000." <i>Emerging Markets Review</i> . 3(1)
97	Claessens, Stijn, Susmita Dasgupta, and Jack Glen. 1995. "The Cross-Section of Stock Returns: Evidence from Emerging Markets." <i>Emerging Markets Quarterly</i> . 2 (4)
98	Brealey, R., Myers, S., and Franklin Allen. 2006. <i>Principles of Corporate Finance</i> . 8 th Edition. New York: McGraw Hill
99	Cochrane, John. 2001. <i>Asset Pricing, Revised Edition</i> . Princeton: Princeton University Press
100	Fama, Eugene F., and Kenneth R. French. 2011. "Size, value and momentum in international stock returns," <i>Journal of Financial Economics</i> . 105 (2012)
101	Damodaran, A. 2012. "Equity Risk Premiums (ERP): Determinants, Estimation and Implications – The 2012 Edition." Updated March 2012. <i>Damodaran Online</i>
102	Damodaran, A. Musing on Markets, "Alternatives to the CAPM: Part 2: Proxy Models," April 29, 2011
103	Pratt, S. (2009), <i>Business Valuation Discounts and Premiums</i> , 2nd ed. John Wiley & Sons
104	Damodaran, A. 2016. "Equity Risk Premiums (ERP): Determinants, Estimation and Implications – The 2016 Edition," Updated March 2016. <i>Damodaran Online</i>
105	Damodaran, A. "What is the risk free rate? A Search for the Basic Building Block," (2008)
106	Copeland, Tom, Tim Koller, and Jack Murrin (1994), <i>Valuation: Measuring and Managing the Value of Companies</i> , 2 nd Ed. New York: John Wiley & Sons
107	Longstaff, F.A. 2004. <i>The Flight-to-Liquidity Premium in U.S. Treasury Bond Prices</i> , <i>Journal of Business</i> , Vol. 77, number 3

Exhibit #	Description
108	Medeiros de Morais, J.F., “The Determinants of Market Interest Rates in Brazil,” Institute of Brazilian Issues, George Washington University, Fall 2008
109	Fabozzi, F. J. (2007), Bond Markets, Analysis, and Strategies, 6th Ed., New Jersey: Pearson Prentice Hall
110	Selected Interest Rates, Federal Reserve of St. Louis, Release H-15
111	2014 Global Entrepreneurship Monitor (GEM) Report
112	Federal Reserve Bank of Philadelphia, 2Q 2016 Survey of Professional Forecasters
113	BLS Consumer Price Index, 2006 - May 2016
114	Google Maps Search: Las Olas Beach Community to El Mistico
115	Google Maps Search: Las Olas Beach Community to Residencias Malaga
116	Google Maps Search: Las Olas Beach Community to Costa del Sol
117	Costa Del Sol Neighborhood Association Homepage
118	Coldwell Banker, Florida Keys Real Estate Market Comparison: January – December 2015 vs. 2014
119	EL Mistico Presentation, June 2016
120	Malaga Residences Presentation, June 2016
121	Email from El Mistico Sales Representative, June 02, 2016
122	HOA Fees Email from EL Mistico Representative, July 21, 2016

APPENDIX B WACC UPDATE

153. I update my estimate of the weighted average cost of capital, which I use to discount the projected free cash flows generated by each business segment under the ongoing concern scenario in my analysis. Although I follow the same methodology as described in Appendix A of my First Report (i.e., the International Capital Asset Pricing Model), I update the calculations to incorporate data available as of June 1, 2016, which results in the following updates:

- a. The risk-free rate, based on the 12-month average yield of the 10-year U.S. Treasury bond has decreased slightly from 2.14% as of November 30, 2015 to 2.08% as of June 1, 2016;
- b. The market risk premium, based on the implied premium computed by Professor Damodaran, has increased from 5.75% as of 2015 to 6.12% as of 2016;¹⁹⁸
- c. The industry beta coefficient, based on the GICS industry code for Diversified Real Estate Activities, has decreased from 1.21 as of November 30, 2015 to 1.14 as of June 1, 2016; the industry debt-to-equity ratio, based on the same industry, has decreased from 143% as of November 30, 2015 to 124% as of June 1, 2016;
- d. The country risk premium, based on the spread of Costa Rica sovereign debt, has increased from 3.6% as of November 30, 2015 to 4.1% as of June 1, 2016.

154. The net result of the updates described above is an increase of the cost of equity from 12.65% as of November 30, 2015 to 13.17%. The after-tax cost of debt, based on the same synthetic approach that I describe in Appendix C.3 of my First Report, has

¹⁹⁸ See Damodaran, Aswath, "Equity Risk Premiums (ERP): Determinants, Estimation and Implications – The 2016 Edition," March 5, 2016, p. 97 (CLEX-104).

increased from 4.78% as of November 30, 2015 to 5.20%.¹⁹⁹ Overall, my WACC estimate has increased from 8.01% as of November 30, 2015 to 8.76% (see Table XII below).

¹⁹⁹ The updated pre-tax cost of debt (7.43%) is the sum of the risk-free rate (2.1%), the industry premium (1.25%, based on the average debt premium estimated by Professor Damodaran for the “Housebuilding,” “REIT,” “Real Estate (Development),” “Real Estate (General/Diversified),” and “Real Estate (Operations & Services)” industries), and the country risk premium (4.1%). See Table XII.

Table XII WACC Update and Comparison

Weighted Average Cost of Capital	Nov-15	Jul-16
Cost of Equity		
Risk Free Rate	2.1%	2.1%
Market Risk Premium	5.8%	6.1%
Beta	1.21	1.14
Raw Beta	1.18	1.10
Beta Levered (Adjusted)	1.12	1.07
D/E US	143.2%	123.9%
Tax Rate US	40%	40%
Unlevered Beta	0.60	0.61
D/E Costa Rica (Same as US)	143.2%	123.9%
Tax Rate Costa Rica	30.0%	30.0%
Country Risk Premium	3.56%	4.10%
Cost of Equity	12.65%	13.17%
Cost of Debt		
Pre Tax Cost of Debt	6.82%	7.43%
Risk Free Rate	2.14%	2.08%
Industry Premium	1.13%	1.25%
Country Risk Premium	3.56%	4.10%
Tax Rate Costa Rica	30%	30%
After Tax Cost of Debt	4.78%	5.20%
WACC	8.01%	8.76%
Debt to Firm Value	59%	55%
Equity to Firm Value	41%	45%

Source: CL WACC Model – Second Report (CLEX-083)