UNITED STATES
CIVILIAN BOARD OF CONTRACT APPEALS

**THIS OPINION WAS INITIALLY ISSUED UNDER PROTECTIVE ORDER AND IS BEING RELEASED TO THE PUBLIC IN ITS ENTIRETY ON APRIL 5, 2021**

GRANTED IN PART: March 26, 2021

CBCA 6012

1125 15TH STREET, LLC,

Appellant,

v.

GENERAL SERVICES ADMINISTRATION,

Respondent.

Brett D. Orlove of Grossberg, Yochelson, Fox & Beyda, LLP, Washington, DC; and Mark H.M. Sosnowsky and Joie C. Hand of Faegre Drinker Biddle & Reath LLP, Washington, DC, counsel for Appellant.

Michael Converse and Elyssa Tanenbaum, Office of the General Counsel, General Services Administration, Washington, DC, counsel for Respondent.

Before Board Judges **HYATT**, **GOODMAN**, and **RUSSELL**.

**RUSSELL**, Board Judge.

Appellant, 1125 15th Street, LLC, seeks damages for the Government's holdover in premises leased by appellant to respondent, General Services Administration (GSA). Respondent has conceded liability under a breach of contract theory, specifically, that the Government breached its implied duty to vacate the premises at the conclusion of the lease. Therefore, the only questions relate to the period of the holdover (specifically, on which date

did the Government vacate the premises), and the amount of any damage award. For reasons stated below, we agree with appellant as to when the holdover period expired. We disagree with both parties as to the fair market rental value of the holdover period, finding that a fair and reasonable rental amount is slightly higher than the amount calculated by GSA's expert. Therefore, we grant the appeal in part.

## Findings of Fact

### The Lease

On April 24, 2006, appellant and the United States, acting through GSA, executed a lease for the use of 64,507 rentable square feet (RSF) of space consisting of the 10th, 11th, and 12th floors at a commercial office building located at 1125 15th Street, N.W., in Washington, D.C. The tenant agency occupying the space was a component of the Department of Homeland Security (DHS). In August 2010, the lease was amended to add 156 RSF for the construction of a guard's room near the loading dock area on the second floor of the building. As a result of that amendment, the total square footage of the leased space increased to 64,663 RSF.

The lease included a security provision allowing the Government, during the lease term, to install and operate X-ray and magnetometer screening equipment in the lobby and loading dock area on the second floor; employ armed guards to screen visitors using the security equipment; and conduct vehicle and passenger searches at the parking garage entrance.

The lease was for a five-year term with a single option to renew for an additional five years. The lease did not include a holdover clause. The lease commenced on or about November 10, 2006, and was set to expire on November 9, 2011. On or about November 7, 2011, the parties executed a supplemental lease agreement under which the Government exercised its five-year option to extend the lease to November 9, 2016. The lease included a base rent amount, plus a pro-rata share for operating expenses and real estate taxes. The base rent amount was the same each year, but the operating expense portion was to be adjusted up or down based on changes in the consumer price index (CPI). Additionally, the real estate taxes were paid in an annual lump sum after the lessor had paid the tax for the year. The annual rent amount for the five-year extension, including adjustments for operating costs and real estate taxes, was $2,579,067.48 per year, or an annual rate of $39.88 per RSF ($2,579,067.48 ÷ 64,663).

Starting in the summer of 2016 and continuing through the summer of 2017, the parties attempted to negotiate a short-term extension of the lease but were unsuccessful. During the negotiations, GSA offered to extend the lease for as much as $50 per RSF for up

to forty-eight months with a right of cancellation after forty-two months. DHS personnel continued to occupy the premises without a lease from November 9, 2016, to December 31, 2018, when DHS moved to another building owned by the same lessor.

GSA's Payments During the Holdover Period

After the lease expired in November 2016, GSA paid rent in the same amount as it had been paying during the final year of the lease, i.e., $214,922.29 per month or an annual rate of $39.88 per RSF. In total, GSA paid the owner $5,523,502.85 in rent for the period November 10, 2016, through December 31, 2018.

The Holdover Period

On January 3, 2019, appellant reported to both GSA and DHS that it had completed a walk-through of the building, that the tenth and twelfth floors still contained government equipment, and that there were still security guards in the building. On or around January 15, 2019, the magnetometer and x-ray machines were removed from the building, but the security guards remained through at least January 17, 2019.

Appellant's Claim and Appeal

On November 7, 2016, appellant filed a claim with GSA's contracting officer requesting that GSA pay fair market rent for the holdover period. On January 26, 2018, appellant filed this appeal as a deemed denial of its claim to the contracting officer. The parties subsequently engaged in extensive discovery and, in February 2020, a hearing was held followed by the parties' filings of post-hearing briefs. The parties presented evidence on their respective positions as to when DHS vacated the building, and expert testimony on the fair market rental value for the holdover period.

Appellant additionally presented testimony from one of its representatives on the amount owed by GSA for real estate taxes due for the holdover period ($134,704.95). The representative also explained that a tenant's operating cost due under the lease was initially based on the tenant's percentage of occupancy of the building, and adjusted in subsequent years based on the CPI. A second representative provided testimony that he was uncertain whether GSA had paid any CPI adjustments to the rental amount for the holdover period.

Evidence on the Holdover Period

As for the holdover period, appellant asserted that it is due rent through January 2019 based on the lease provision attaching the right of the Government to maintain security in the building with the lease period. The provision allowed "the Government to install . . . security measures during the term of the [l]ease." Specifically, part of the rent included allowing the

Government to place armed guards in the lobby and near the second floor loading dock of the leased premises, and to install and operate x-ray and magnetometer screening equipment.

To support its position that appellant suffered no compensable injury due to the presence of the security guards and equipment at the property in January 2019, GSA elicited testimony from one of appellant's representative that appellant did not have a tenant lined up to take over the space in January 2019. The witness additionally acknowledged that the continued presence of the security guards did not prevent appellant from renting the space on the floors vacated by DHS personnel, and that tours for prospective tenants could have occurred in January 2019.

Evidence on Fair Market Rent

Daniel Klueger, a commercial real estate broker, was appellant's expert. During the hearing, Mr. Klueger admitted that he is not a real estate appraiser, is unfamiliar with certain appraisal standards, including those in the Uniform Standards of Professional Appraisal Practice, and has no experience with federal government leases.

Mr. Klueger opined that the holdover rent should be around $60 per RSF, or 150 % of the rent that GSA paid under the lease. In his expert report, he stated:

> The GSA should pay 150% of the then base rent consistent with industry standards. In my twelve (12) year career in representing Tenants and reading leases that had been negotiated by real estate brokers and advisers of all kinds, every lease that I've read has a definition for what happens if the Tenant does not vacate and stays beyond the stated Lease Expiration Date – this period is known as Holdover. The market holdover clause is between 150% of the then escalated rent (including additional rent) to 200% of the then escalated rent (including additional rent).

He additionally noted that, in the Washington, D.C., commercial real estate market, tenants pay a premium for a short-term lease. He asserted that:

> Tenants buy flexibility. In this case, GSA unilaterally imposed on the Landlord a flexible, two-year solution for the GSA, and an above market rent should be charged to the GSA for that flexible term.

Mr. Klueger explained that he spoke with three brokers and, based on those conversations, concluded that a short-term lease would include a premium of between ten and fifteen percent attached to the asking rate.

Appellant also presented testimony from a GSA contracting officer responsible for GSA's efforts to negotiate an extension of the lease at the 1125 15th Street building. The

contracting officer stated that, in September and November 2016 (before the expiration of the lease), GSA made two offers, the first at $47.25 per RSF and the second for $49 per RSF, to continue renting the space for a twenty-four-month period. The contracting officer explained that the agency arrived at that figure based on reviewing comparable rents in the area of the leased premises. However, the contracting officer also stated that GSA would not have made the offers but for the effort to resolve the issue of DHS's occupancy of the building in holdover status.

A second GSA contracting officer, also called by appellant, provided testimony that the Government does not typically include a holdover clause in its leases. He added that, to end the holdover at the 1125 15th Street property, GSA leased space for DHS at another building owned by appellant in Washington, D.C. The contracting officer explained that GSA paid $50 per RSF under the new lease, but would not have paid this amount absent the agency's motivation to end the holdover at the 1125 15th Street building.

GSA presented expert testimony from David C. Lennhoff on the fair market rental value for the holdover period. Mr. Lennhoff is certified as a real estate appraiser in the District of Columbia, has written sections of a book on appraising real estate, and teaches on the subject of appraising internationally. He has experience appraising commercial properties for the purpose of estimating fair market value and fair market rental value for both property owners and tenants in holdover.

In appraising the holdover value of the property, Mr. Lennhoff applied the standards contained in the Uniform Standards of Professional Appraisal Practice. He defined market rental value as an amount that a "landlord would accept and a renting tenant would pay, both being reasonably knowledgeable and under no compulsion to have to [effectuate the] rent[al]." He explained that the primary method of determining market rental value for a particular property is to consider the rental value of comparable properties.

Mr. Lennhoff completed two appraisal reports on the property – the first in or around January 2018 in which he concluded that the property was valued at $38.02 per RSF and the second in 2019 in which he valued the property at $39.96 per RSF. In the second report, he considered a holdover period with a potential length of between twenty-two months and four years, and also included an adjustment for the uncertainty of the holdover duration. For data, he looked at two sources, CoStar, which mostly provides the list asking price for properties, and CompStak, which provides information on consummated deals like leases. He explained that he examined "hundreds of leases" in CompStak. In determining the effective or comparable rent, he started with the nominal or face rent of the properties and then adjusted for factors like variations in lease terms, tenant improvements, concessions (e.g., free rent), when the lease occurred, class of building, size of the leased space, and location of the property (e.g., proximity to public transportation). Mr. Lennhoff also stated that he considered the presence of the magnetometer, concluding that the presence of the equipment would not change the rent that a landlord would receive. Mr. Lennhoff's analysis regarding

rental value for the holdover period did not account for increases in real estate taxes beyond those paid during the first or base year.

Mr. Lennhoff made a positive adjustment of five percent to the rental value of all comparable properties to account for the uncertainty of the holdover duration. However, he admitted that he relied on anecdotal information from two real estate sources as the basis for this adjustment. Neither source provided a specific figure as to a percentage that should be added to an effective rent to adjust for the uncertainty of a holdover duration, only offering that the tenant would "have to pay a little bit more in rent."

At the hearing and in its post-hearing briefing, GSA argued that DHS's holdover of the leased space did not cause appellant harm for which appellant is entitled to any additional compensation. In support, GSA noted that it had paid monthly rent to appellant during the holdover period not in dispute (i.e., November 10, 2016, to December 31, 2018) equaling the amount set out in the expired lease. The lease amount, $39.88 per RSF, was close to the $39.96 per RSF amount that Mr. Lennhoff had opined was the fair market rental value for the leased space during the holdover period.

GSA also attempted to show that appellant could not have rented the space occupied by DHS during the holdover period for an amount greater, let alone substantially greater, than what GSA had paid. GSA elicited testimony from one of appellant's representatives that, in December 2015, about eleven months before the DHS lease was set to expire, appellant was unsuccessful in obtaining a lease from another federal agency to rent space on lower floors in the building. The witness testified that appellant had offered to rent the space for $35.22 per square foot for a fifteen-year period, an amount considerably lower than the $39.88 per RSF that GSA paid during the holdover period. Further, GSA presented evidence showing that space in the building remained empty for many years. GSA showed that, when a prior government tenant moved out of the 5th through 7th floors in 2011, the building owner left that space empty, and it was still empty nine years later at the time of the hearing.

## Discussion

It is well settled that "[t]o recover for breach of contract, a party must allege and establish: (1) a valid contract between the parties, (2) an obligation or duty arising out of the contract, (3) a breach of that duty, and (4) damages caused by the breach." *San Carlos Irrigation & Drainage District v. United States*, 877 F.2d 957, 959 (Fed. Cir. 1989). As for the first and second factors, to establish breach for a holdover tenancy, the United States Court of Appeals for the Federal Circuit has explained that, "[although] a lease [agreement] may concern and convey a property interest[,] it is also very much a contract" and, further, "due to [the] definite term of [a] lease and the nature of the landlord-tenant relationship, an implied duty to vacate is an inherent part of every fixed term lease agreement unless the parties explicitly express an intention to the contrary." *Prudential Insurance Co. of America v. United States*, 801 F.2d 1295, 1298-99 (Fed. Cir. 1986). As against the Government, this

implied duty to vacate is premised under a "contract implied in fact." *Cameron University*, DOT BCA 2010, 90-3 BCA ¶ 23,079 (noting that, under the Contract Disputes Act, the board "do[es] not possess jurisdiction to hear claims founded upon contracts implied in law," but that "the remedy of quantum meruit – the reasonable value in the marketplace of the services rendered – may be applied to cases founded upon a contract implied in fact."). The Government breaches its implied duty to vacate property by holding over beyond the lease term. *Prudential Insurance Co*., 801 F.2d at 1300.

On the issue of damages, the United States Court of Claims, the predecessor to the Federal Circuit, has explained that the court has "long recognized that one who occupies the premises of another does so, absent contrary agreement, with the implied obligation to pay a reasonable rental therefor." *Yachts America, Inc. v. United States*, 673 F.2d 356, 365 (Ct. Cl. 1982); *see also Garrity v. United States*, 67 F. Supp. 821, 826 (Ct. Cl. 1946) (In the absence of an agreement governing the holdover term, a lessor is entitled "to recover the reasonable rental value of the premises for the period they were actually occupied by [the lessee/holdover tenant] after the termination date of the old lease."). One of our predecessor boards determined that damages may be based on the rent paid under the lease agreement prior to breach, or the fair market rental value. *Cafritz Co. v. General Services Administration*, GSBCA 13525-REM, 98-2 BCA ¶ 29,936 (an appropriate remedy for the Government's holdover of lease space is "the fair market rental value of the premises for the holdover period less what . . . has [already been] paid [to the] appellant during the holdover period."); *Rupert v. General Services Administration*, GSBCA 10523, 93-1 BCA ¶ 25,243 ("The rent in the lease is evidence of rental value, but a landlord may establish a rental value greater than rent.").

The issues that we must decide in this appeal are (1) whether the holdover period expired at the end of December 2018 or January 2019, and (2) damages, given that GSA has conceded liability.

The Holdover Period

As for the question of the holdover period, appellant maintains that the Government was in holdover through January 2019 when the security equipment was removed and the security guards were no longer on the premises. GSA maintains that the holdover period extended only through December 2018 when DHS personnel vacated the premises. GSA argues that appellant suffered no damage due to the presence of the security equipment and guards on the premises through January 2019. In support, GSA relies on *Cafritz,* in which the board determined that leftover furnishings on property did not extend a holdover tenancy because the items did not "affect[] the appellant's use and occupancy" of the property. GSA points to evidence showing that the continued presence of the guards as well as the equipment in the lobby and near the second floor loading dock area did not prevent appellant

from renting space on the 10th, 11th, and 12th floors vacated by DHS or conducting tours for prospective tenants on those floors.

We would find GSA's argument persuasive except that the lease agreement at issue in this appeal attaches the Government's right to maintain security in the building with the duration of the lease. The specific lease term states, "Lessor agrees to allow the Government to install . . . security measures *during the term of the Lease*." (Emphasis added.) The record is unclear why the Government did not remove the security in December 2018 when DHS personnel vacated the building. Regardless, under the lease agreement, appellant received consideration for permitting the Government to maintain armed guards and operate x-ray and magnetometer screening equipment in the building. Specifically, the rent included payment permitting the Government to maintain the security presence. Accordingly, we find that appellant's entitlement to rent was not extinguished when DHS personnel vacated the building in December 2018, but when the security was removed in January 2019. *See Yachts America, Inc.*, 673 F.2d at 365 ("[W]hen a lessee holds over without [a] new agreement after the expiration of [its] lease, the terms of the old lease agreement apply.").

Damages

Fair Rental Value

GSA does not dispute that appellant is entitled to the fair market rental value for DHS's occupancy of appellant's property during the holdover period. However, the parties disagree on the amount owed. Although the evidence shows the shortcomings of both parties' analyses on fair market value, we find the analysis offered by GSA's expert to be the most helpful and persuasive on the issue.

In determining a value for the holdover tenancy, Mr. Klueger, appellant's expert, opined that GSA should pay around $60 per RSF, or 150 % of the base rent paid under lease which he asserted is the industry standard. He looked generally at what a month-to-month, holdover tenancy provision in a commercial lease might entail. In his expert report, he explained that, "[i]n his twelve year career. . . representing [t]enants and reading leases that had been negotiated by real estate brokers and advisors of all kinds, every lease that [he has] read has a definition for what happens if the [t]enant does not vacate and stays beyond the stated Lease Expiration Date . . . . The market holdover clause is between 150% of the then escalated rent (including additional rent) to 200 % of the then escalated rent. . . ." However, assuming that commercial leases effectuated in the Washington, D.C., area typically include such a provision as Mr. Klueger opines, we are unpersuaded that this "industry standard" is a reliable proxy to assess damages in this appeal. As an initial matter, the standard does not evidence reasonable rental or fair market value. "Fair market value has been defined in various ways." *Miller v. United States*, 620 F.2d 812, 825 (Ct. Cl. 1980). However, a frequently quoted definition was set out in *Jack Daniel Distillery v. United States*, 379 F.2d

569 (Ct. Cl. 1967). In that case, the court stated, "The legal definition of fair market value is the price at which property would change hands in a transaction between a willing buyer and a willing seller, neither being under compulsion to buy or sell, and both being reasonably informed as to all relevant facts." *Id*. at 574. Rent payments made under a commercial holdover clause, in the substantially inflated range of 150 to 200 % of the base rent paid under an expired lease, seem inconsistent with the idea of a "reasonable rental" for a property. *Garrity*, 67 F. Supp. at 826.

Further, notwithstanding appellant's evidence as to the inclusion of a holdover provision in commercial leases, we have no record of rental amounts actually paid by a commercial lessee in holdover status. We are also disinclined to use what has been proffered as a standard holdover provision in commercial leases as a basis for a monetary remedy in this appeal, given the GSA contracting officer's testimony that federal leases typically do not include a holdover provision. Thus, we find that appellant's evidence based on a commercial holdover clause that would likely not be included in a federal lease is inapposite or too speculative to support a reasonable finding of entitlement to $60 per RSF as damages for the holdover period. We note that such an award would likely result in an unfair windfall to appellant and, therefore, will not be made.

Additionally, as already stated, a predecessor board has previously determined that an appropriate remedy for the Government's holdover of lease space is "the fair market rental value of the premises," less any amount that has already been paid to the appellant. *Cafritz*. One method of determining "fair market rental value" is to look at rents paid in the same market for space comparable to the one at issue in the litigation. *Id*.; *see also Norman v. United States*, 63 Fed. Cl. 231, 270 (2004) ("The fair market value of property is most traditionally and frequently calculated using the comparative sales approach"); *Good v. United States*, 39 Fed. Cl. 81, 106 (1997) (use of the "sales comparison approach" is the "most reliable method of arriving at the fair market value").

We find the analysis and opinions provided by Mr. Lennhoff, an experienced and certified appraiser, to be particularly persuasive on the issue of fair market rental value. In his report and testimony, Mr. Lennhoff defined market rental value similar to that set out in *Jack Daniel Distillery*, i.e., as an amount that a "landlord would accept and a renting tenant would pay, both being reasonably knowledgeable and under no compulsion to have to rent." To determine the fair market rental value of the 1125 15th Street property, Mr. Lennhoff examined hundreds of leases and, to account for a holdover term, assumed a term as short as twenty-two months and as long as four years. Similar to the appraiser in *Cafritz*, to determine the effective or comparable rent of the properties considered, Mr. Lennhoff started with the nominal or face rent of the properties and then, to account for the different characteristics and features of the properties, made adjustments for factors like tenant improvements, concessions (e.g., free rent), when the lease occurred, class of building, size of the leased space, and location of the property (e.g., proximity to public transportation).

*See Cafritz* (noting that GSA's appraiser "adjusted the rental rate for the comparables based upon their location and building quality in order to produce an 'apples-to-apples' comparison").

Mr. Lennhoff prepared two appraisal reports. In the second report, completed in 2019, he made an adjustment to account for the uncertainty of a holdover tenancy. Based on his analysis, Mr. Lennhoff opined that the fair market rental value of the office space at 1125 15th Street, beginning on November 10, 2016, was $39.96 per RSF inclusive of a five percent premium to account for the uncertainty of the holdover period.

Both experts concluded that appellant was entitled to an adjustment of the effective rent specifically to account for the uncertainty of a holdover period, and both primarily relied on fairly limited anecdotal evidence provided by other brokers to opine on what that adjustment should be. Based on conversations with three brokers, Mr. Klueger explained that tenants in the Washington, D.C., area pay a premium of between ten and fifteen percent for a flexible lease term, like a short-term or holdover lease. To support his assessment of a five percent adjustment for the uncertainty of a holdover lease, Mr. Lennhoff relied on conversations that he had with two real estate contacts. Mr. Lennhoff testified that he did not receive a solid answer to his question about an amount or percentage that would be paid over the asking rent for a holdover term, only that the tenant would "have to pay a little bit more in rent." Given that both experts agree that appellant is entitled to some compensation for the uncertainty of a holdover tenancy and rely on the same type of information to support their respective positions (i.e., anecdotal), we afford both opinions some consideration. Mr. Lennhoff found that the fair market rental value of the holdover tenancy was $39.96 per RSF inclusive of his assessment of a five percent premium for the uncertainty of the holdover period. To afford some consideration to Mr. Klueger's opinion on the issue, we find that the fair market rental value of the holdover tenancy is $41.96 per RSF, adding an additional five percent to Mr. Lennhoff's assessment (i.e., $39.96 x 1.05).

However, we are unpersuaded by both appellant's other arguments in support of a higher amount and respondent's argument that appellant is not entitled to damages. Both parties rely on unaccepted offers to rent to make their case. We find such evidence unpersuasive to show fair market rental value. *See, e.g.*, *Missouri Baptist Hospital v. United States*, 213 Ct. Cl. 505, 527 (1977) ("Evidence of an offer is inadmissible to prove fair market value."). Specifically, we will not, as appellant urges, consider the amounts that GSA offered during the parties' attempts to resolve the holdover, in the range of $50 per RSF, as an indication of fair market rental value. Further, the record does show that GSA's offers were based on at least one other factor in addition to fair market rental value. Specifically, GSA's contracting officers both provided testimony that the agency would not have made such substantial offers but for the agency's motivation to end the holdover tenancy. Finally, we will not, as respondent urges, consider appellant's effort to rent other space at the building, including its offer to a potential tenant to rent space at $35.22 per square foot

(which is lower than the $39.88 per RSF paid by GSA during the holdover period), as an indication of fair market rental value for the space that was occupied by DHS.

Real Estate Taxes and Operating Costs

Appellant presented undisputed testimony from one of its representatives that GSA owed $134,704.95 in real estate taxes for the holdover period. The representative also explained that GSA was obligated, during tenancy, to pay a pro rata share for operating costs adjusted annually based on the CPI. A second representative provided testimony that he was uncertain whether GSA paid any CPI adjustments to the rental amount for the holdover period. We find that appellant is entitled to both the unpaid real estate tax amount and any operating costs due under the lease.

## Decision

The appeal is **GRANTED IN PART**. Appellant is entitled to rent of $41.96 per RSF for the holdover term of November 10, 2016, to January 31, 2019 (minus rent that GSA has already paid), $134,704.95 in real estate taxes, any unpaid operating costs, and interest under the Contract Disputes Act, 41 U.S.C. § 7109(a) (2018), calculated from November 7, 2016, the date on which appellant submitted its claim to the contracting officer, through the date that the award is paid.

Beverly M. Russell
BEVERLY M. RUSSELL
Board Judge

We concur:

Catherine B. Hyatt
CATHERINE B. HYATT
Board Judge

Allan H. Goodman
ALLAN H. GOODMAN
Board Judge