

## Publications

### *The Evaluator: Summer 2021 Valuation Analyses*

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### Valuation Headlines

#### **CALIFORNIA COURT UPHOLDS CITY ORDINANCE THAT ASSESSES DIFFERENT TRANSFER FEES BASED UPON THE CONSIDERATION PAID**

*Ashford Hospitality v. City and County of San Francisco*, Court of Appeal, 1<sup>st</sup> Appellate Dist., 4<sup>th</sup> Div. 2021.

Ashford Hospitality (Ashford) acquired a majority interest in a property located on 2nd Street in San Francisco. The acquisition resulted in a change in ownership and as a result, Ashford paid \$3,348,025 in transfer taxes based upon the \$133,920,700 self-report value of the property at transfer. Ashford then filed an administrative claim seeking a refund for the transfer tax. After the city failed to act on the refund claim, Ashford filed a lawsuit seeking a refund of the total amount paid. Ashford's complaint alleged that the tiered transfer tax was unconstitutional and it was improper to levy a different rate of tax based upon the amount of the transfer. The trial court found that it was rational for the city "to treat the sale of transfer of a higher valued property differently from the sale of a lower valued property."

The appellate court affirmed the trial court's decision finding that the city's reasoning, including the owner's ability to pay, and the time and costs associated with the city's audits for the self-reported transfer tax, may be more costly for a higher valued property.

#### **NEW YORK COURT RULES THAT THE COVID-19 PANDEMIC DID NOT LOWER A MALL'S FAIR MARKET VALUATION FOR TAXATION PURPOSES**

*In the Matter of Crystal Run Galleria LLC et al. v. Town of Wallkill*, 2021 NY Slip Opinion 21006, Orange County Supreme Court, (January 20, 2021).

The owner of a regional mall challenged the town's tax year 2020 assessment for the property on the basis that the COVID-19 pandemic had caused its fair market value to decline. The mall owner had previously entered into a consent order with the town that fixed the fair market value of the property at \$132,738,000 for tax years 2018, 2019, 2020, and 2021. The consent order contained an exception that allowed for the stipulated fair market value to be reduced if the property is altered by "fire, destruction, related demolition, or similar catastrophe."

The mall owner asserted that the COVID-19 pandemic should be considered a catastrophe. An executive order from the Governor closed the mall, considered a non-essential business, from March 19, 2020 through July 10, 2020. The mall owner argued that the property was worth significantly less than the town's assessment as a result. Meanwhile, the town argued that the mall's arguments did not qualify for the exception because the mall had not been altered by fire or destruction and that an "economic" event does not fall under the definition.

In upholding the town's assessment, the Court held that the catastrophe exception to the consent order's assessment lock is not applicable to the circumstances created by the COVID-19 pandemic. The Court noted that the COVID-19 pandemic "may well have financially impacted the profitability and value" of the mall but that the pandemic "had not, as yet, altered the 'condition' of the property...". The Court further explained that the property was functioning as an open and intact shopping mall on both the taxable status date and the Section 301 valuation date. As a result, the Court concluded that the financial impact from the pandemic is wholly irrelevant to determining the Property's assessed value for purposes of the tax year 2020 assessment roll.

### **COLORADO LAW CHANGE NOW PERMITS STATE BOARD OF ASSESSMENT APPEALS TO INCREASE ASSESSMENT ON APPEAL**

Colorado HB 21-1083, effective April 7, 2021.

On April 7, 2021 the Colorado Governor signed House Bill 21-1083, which removes a restriction on increasing real property valuation during the appeal process. Prior to the enactment of this legislation, the valuation of a property could not be adjusted to a value higher than the valuation set by the County Board of Equalization. This legislation may result in fewer appeals filed because taxpayers may not want to risk the value of their real property being increased as a result of pursuing an appeal.

### **TENNESSEE STATE BOARD OF EQUALIZATION CONFIRMS THAT TAX CREDITS MUST BE INCLUDED IN THE VALUATION OF LOW-INCOME HOUSING TAX CREDIT PROPERTIES**

*In re Ford Creek Village LP*, Tennessee State Board of Equalization, Appeal Nos. 112079 and 127963 (Feb. 16, 2021).

The Tennessee State Board of Equalization (SBOE) recently rejected a taxpayer's valuation challenge of a Low-Income Housing Tax Credit (LIHTC) project in Jonesborough, specifically confirming that tax credits must be included in the valuation of low-income housing properties. Though the taxpayer attempted to rely on case law from Georgia and the United States Supreme Court to support his position that tax credits should not be included, the SBOE rejected this argument, noting that the referenced decisions were not controlling in Tennessee.

Instead, citing to existing SBOE rules that require inclusion of the tax credits, along with precedent from the state Court of Appeals, the SBOE ruled that a proposed valuation for a low-income housing project must include the tax credits. Because the taxpayer failed to provide a proposed valuation that included the credits, the SBOE determined that he had failed to meet his burden of proof. The SBOE instead adopted the County Assessor's proposed valuation, as the Assessor had provided a comprehensive analysis that included the low-income housing tax credits.

#### **IOWA COURT AFFIRMS COUNTY'S VALUATION OF A LOWE'S BASED ON ITS PRESENT USE RATHER THAN ITS FAIR MARKET VALUE**

*Lowe's Home Centers, LLC v. Iowa Property Assessment Appeal Board*, No. 20-0764 (Iowa Ct. App. 2021), February 17, 2021.

The Johnson County Assessor had valued a Lowe's at \$11,800,000. Lowe's had challenged the County's original assessment with the County Board of Review, which did not change the County's value. Lowe's then appealed the decision to the Iowa Property Assessment Appeal Board (PAAB). At the PAAB hearing, Lowe's presented an appraisal and expert testimony that valued the property at \$5,200,000. Lowe's appraiser valued the property as if it were vacant and relied primarily on a sales comparison approach that contained sales for stores that were all vacant at the time of sale.

The County presented an appraisal and expert testimony that valued the property at \$10,940,000. The County's appraiser valued the property as if it was occupied. The PAAB adopted the County appraiser's valuation and found that Lowe's appraiser failed to make adjustments that were necessary to valuing the fee simple interest of the property in its current use. Following an appeal of the PAAB's decision, the district court affirmed the decision and Lowe's then appealed to the Iowa Court of Appeals.

In upholding the County's valuation for the Lowe's, the Court of Appeals affirmed that the County's consideration of the current use of the property did not violate Iowa law. Citing precedent, the Court of Appeals noted that "an assessor must...consider conditions existing at the time and the condition of the property in which the owner holds it." The Court rejected Lowe's contention that a fee simple interest must be valued as vacant and agreed with the district court's conclusion that the PAAB's denial of Lowe's appraisal methodology was appropriate.

### **Other Valuation Headlines of Note**

#### **IN REVIEW OF ASSESSMENT OF BIG BOX STORE, KANSAS COURT OF APPEALS REAFFIRMS PRECEDENT THAT BUILD TO SUIT LEASES MUST BE APPROPRIATELY ADJUSTED TO BE UTILIZED FOR DETERMINING VALUE**

*In re: Arciterra BP Olathe KS, LLC*, No. 121,438, Kan. Ct. App. (April 2, 2021).

The Taxpayer, a big box retailer, constructed its improvements in 2005 subject to a 20-year build-to-suit lease. The lease also gave the Taxpayer the option to buy the property for \$10 at the termination of the lease period. The Taxpayer appealed its assessment for tax year 2016 and 2017 to the Board of Tax Appeals (BOTA). At BOTA, the parties presented competing appraisals regarding the valuation of the subject property. On consideration of the appraisals, BOTA substantially reduced the assessment of the subject

property for 2016 and 2017.

On appeal, the County criticized BOTA's adoption of the Taxpayer's appraisal. The Taxpayer's appraiser did not use any first generation build-to-suit leases because he commented they are more like financing arrangements and are not likely representative of market rent. The Taxpayer's appraisal provided BOTA with a valuation as a "hypothetical leased fee" estate. Using this method, the Taxpayer's appraisal assumed the property would be encumbered by a short-term lease agreement with a moderate credit tenant. The Court noted that this method was to value a property's fee simple interest while accounting for its current occupancy. While BOTA ultimately adopted this hypothetical leased fee value, the Court did not review whether such a value was proper because the County did not preserve that issue on appeal.

The County's appraiser utilized build-to-suit leases in determining market rent. The County's appraiser made adjustments to those build-to-suit leases in his analysis. But BOTA, relying on its decision in *In re Equalization Appeal of Prieb Properties*, 47 Kan. App. 2d 122, 275 P.3d 56 (2012), found that the County's appraiser failed to show he adjusted build-to-suit leases sufficiently to reflect market rent.

The Court found that the BOTA properly relied on the Taxpayer's appraisal to find that the property was properly valued at \$9,070,000 in 2016 and \$9,410,000 for 2017.

#### **MICHIGAN COURT OF APPEALS UPHOLDS MICHIGAN TAX TRIBUNAL'S DECISION DETERMINING VALUATION OF UPSCALE CONTINUING CARE RETIREMENT COMMUNITY**

*DRSN Real Estate GP, LLC v. City of Grosse Pointe Woods*, Mich. Ct. App., Dkt. No. 352153, 01/28/2021 (unpublished).

The Michigan Court of Appeals reviewed the Michigan Tax Tribunal's (Tribunal) decision regarding valuation of a newly constructed continuing care retirement community (CCRC). The Court, remanded on two discrete issues, but in large part, upheld the Tribunal's acceptance of the City's methodology for valuing the CCRC.

The CCRC contained three levels of housing – independent living units, assisted living units, and skilled nursing units. The improvements were constructed from 2013 to 2015 and contained upscale amenities. The property was financed through the issuance of two municipal bonds, one taxable and one non-taxable. The CCRC appealed the City Assessor's determination of the true cash value to the MTT. Over the course of the six-day hearing, the CCRC presented evidence of valuations using the sales-comparison approach, the cost-minus-depreciation approach, and the income-capitalization approach. The City's expert based his valuation solely on the cost approach.

The Court held that the Tribunal made two errors in its decision. Specifically, the Tribunal: (1) improperly increased the taxable value for 2017 as the property was subject to the multiplier limitation because there was no new construction or additions in 2016 and (2) failed to subtract demolition costs from land value. The Court remanded the case on both of these issues.

On the remaining issues related to the valuation determination, the Court upheld the Tribunal's determinations.

- **Costs Associated with Financing.** The Tribunal did not err when it included certain indirect costs associated with the costs of obtaining financing in its calculation of value. The Taxpayer argued that the costs associated with obtaining financing through the bond issuance should not have been included in the cost-approach calculation because they were costs of financing that did not add value to the property. The taxpayer contended it incurred substantially higher costs in obtaining the bond financing than it would have incurred through conventional bank financing. The Court noted that these were necessary expenditures to complete the project because there was testimony that bank financing was not available.
- **Land Use Restriction Agreement.** The Taxpayer contended that the Tribunal erred when it failed to consider the land use restriction agreement, which required 16 of the independent living units to be used for qualified low-income tenants. The Court held that the Tribunal did not err because the Taxpayer's expert did not present sufficient evidence to demonstrate an alleged detriment to the subject property's value.
- **Contractor Profit.** The Court also disagreed with the Taxpayer that the Tribunal improperly included a contractor's profit based on a percentage of contractor cost, even when part of those costs was paid by the Taxpayer.
- **Economic and Functional Obsolescence.** The Court agreed with the Tribunal that the Taxpayer did not prove any functional or economic obsolescence because there was no evidence that the property was "over-built." The record indicated that the CCRC had the ambiance of a luxury hotel, which took into account the market tastes and needs.
- **Vacant and Available.** The Court rejected the petitioner's argument that the property had to be valued as vacant and available. The relevant statute did not incorporate such a standard and the Tribunal did not ignore this distinction when it discredited the Taxpayer's sales that had over-reliance on sales of CCRCs that were going concerns. The Court upheld the Tribunal's determination that the Taxpayer's comparative sales and income analyses were unreliable and entitled to no weight.

#### NEBRASKA TAX EQUALIZATION AND REVIEW COMMISSION REJECTS VALUATION OF COMMERCIAL PROPERTY BASED ON SALE-LEASEBACK TRANSACTION

*Hurd Kearney, LLC & Hy-Vee, Inc. v. Buffalo Cty. Bd. of Equalization* (Dec. 9, 2020, NE. Bd. of Equalization and Review Comm. Case No. 18C 0144).

The Nebraska Tax Equalization and Review Commission (Commission) overturned a county assessment that relied upon a sale-leaseback transaction. The matter involved a 1.46 acre parcel improved with a supermarket, convenience store, and car wash. The improvements were completed in 2016, at which time the owner entered into a sale-leaseback transaction, in which it sold the property for \$15,292,915 and immediately entered into a 20-year lease at a rate that was higher than market.

For tax year 2018, the county valued the property at \$13,896,935. The owner appealed to the county board of review, asserting a value of \$7,392,900. The owner provided appraisal evidence using all three approaches to value. In doing so, the appraiser selected only sales and rent comparable that were unaffected by sale-leaseback transactions or build-to-suit arrangements. The county also provided appraisal evidence. The county appraiser did not exclude sales and rents that were affected by sale-leaseback transactions or build-to-suit arrangements. At least two of the rent comparables were build-to-suit arrangements, and

four sale comparables were disqualified by the county assessor as being non-arm's-length.

The Commission found that the owner presented more reliable evidence of value. In adopting the owner's appraised value of \$5,970,000, the Commission found that the sale-leaseback purchase price and lease rate were not reflective of the fee simple interest of the property. The Commission stated that reliance should not be placed on sales and rent comparables that are affected by sale-leaseback and build-to-suit arrangements: "What they purchased was not the entire bundle of rights, but rather, the rights to collect above-market rent on the property during the lease and to sell, lease, or occupy the property at the end of the lease. \*\*\* [S]ale-leaseback transactions 'are actually financing vehicles' [impacting] both the income and the sales comparison approaches to value because Nebraska law requires special financing considerations to be considered in determining what constitutes a comparable sale."

### **TENNESSEE APPEALS COURT FINDS THAT AN INTERSTATE PIPELINE WAS PROPERLY ASSESSED AS REAL PROPERTY RATHER THAN PERSONAL PROPERTY**

*Colonial Pipeline Co. v. TN State Bd. of Equalization* (Jan. 25, 2021), Court of Appeals Case No. M2020-00247-COA-R12-CV.

A Tennessee appeals court affirmed a decision of the Tennessee Board of Equalization denying the Pipeline's claim that its interstate pipeline should be classified as personal property rather than real property. Tennessee personal property is assessed at a lower rate than real property.

The Pipeline argued that classifying its pipelines as real property violated the state's equal protection clause because locally assessed pipes, which included pipes related to above-ground tanks at petroleum storage facilities or which were related to manufacturing, were treated as personal property.

The Court found that plain language of the state's definition of real property supported the classifications. Under Tenn. Code 67-5-501(10)(B)(iii), real property includes "[m]ains, pipes, and tanks permitted or authorized to be built, laid or placed in, upon, or under any public or private street or place \*\*\*" The Pipeline's property was determined to fall under the definition of real property because the Pipeline's property was placed pursuant to easements. "The words 'permitted or authorized' [under the statute] include pipelines placed on or under property pursuant to easements: the easements permit or authorize Colonial to build or place its pipeline under the property owner's land." *Id.* at 5.

In contrast, the locally assessed pipes were classified as personal property because "[p]iping installed on land owned in fee simple by the piping owner does not require legal approval and thus does not fall within the plain meaning of the statutory language." *Id.* at 6. In conclusion, there was no violation of the state's Constitutional Equal Protection provisions.

### **PENDING TEXAS BILL WOULD FREEZE PROPERTY VALUES AT CURRENT LEVEL UNTIL SOLD, TRANSFERRED OR IMPROVED**

Texas House Bill 4024, which was introduced in March of 2021, would prevent certain property-tax increases by freezing the taxable value of properties across the state at their current levels. Under the bill, property taxes will be locked in at the current appraised value and will remain there until a property is sold or transferred or improvements are made on the property. If a property owner chooses not to disclose a

sales price, the current appraisal and tax process will continue to apply. The bill was referred to the House Ways and Means Committee on March 29, 2021 and has not progressed since that date.