

PROPERTY ASSESSMENT APPEAL BOARD

ORDER ON REMAND

PAAB Docket Nos. 2015-052-00558C & 2016-052-00055C

Parcel No. 0636277003

Wal-Mart Real Estate Business Trust,

Appellant,

vs.

Johnson County Board of Review,

Appellee.

Introduction and Procedural Background

Wal-Mart Real Estate Business Trust is the owner of a commercial retail property located at 2801 Commerce Drive, Coralville.

The property's January 1, 2015 assessment was set at \$16,938,900, allocated as \$8,887,300 in land value and \$8,051,600 in improvement value. The Johnson County Assessor subsequently modified the 2015 assessment to reflect a small portion of the site that was conveyed to the City of Coralville in the spring of 2015 for the purpose of building a new traffic roundabout. After the reduction, the final valuation for the entire Wal-Mart property for 2015 was \$16,915,900, allocated as \$8,864,300 in land value and \$8,051,600 in improvement value.

The January 1, 2016 assessment was set at \$16,916,200, which reflects a \$300 increase attributed to the improvements. (Appellee Post Hearing Brf, p. 2; Exs. 3, 6, & 10).

Wal-Mart petitioned the Board of Review claiming the property was assessed for more than the value authorized by law under Iowa Code section 441.37(1)(a)(1)(b) (2015) for both 2015 and 2016. (Ex. 3 & 6). The Board of Review denied the petitions.

Wal-Mart then appealed to PAAB. This appeal came on for hearing before PAAB on May 3, 2017. Attorneys Paul Burns and Melissa Carrington represented Wal-Mart Real Estate Business Trust. Assistant Johnson County Attorney Susan Nehring represented the Board of Review.

On September 29, 2017, PAAB issued an order modifying the property's assessment for both 2015 and 2016 to \$15,500,000. In coming to that conclusion, PAAB gave equal weight to appraisals completed by Chris Jenkins and Keith Westercamp, finding them both persuasive, and concluded the fair market value of the property as of the assessment dates was a value between the two appraisals' reconciled values.

Wal-Mart timely filed a petition for judicial review in the Johnson County District Court challenging the PAAB order. The District Court issued its ruling on August 30, 2018, and remanded the matter to PAAB.

In its ruling, the District Court found that PAAB erred "in concluding that comparable sales data were not available or readily ascertainable without requiring that Johnson County prove as much by a preponderance of the evidence." (D. Ct. Ruling p. 6). The District Court also concluded that PAAB used a decision-making process prohibited by law and "should have either decided which expert analysis to rely on in coming to a final conclusion or found that Johnson County had failed to carry its burden." (D. Ct. Ruling p. 9). The District Court rejected Wal-Mart's argument that consideration of creditworthiness in valuation amounts to a violation of the special use prohibition in Iowa Code section 441.21(2). The parties filed post-ruling motions under Iowa Rule of Civil Procedure 1.904, which the Court denied.

Upon consideration of the District Court ruling and its remand to PAAB, PAAB issues these Findings of Fact and Conclusions of Law.

Findings of Fact

The following Findings of Fact are substantially similar to the PAAB Order issued on September 29, 2017. Footnotes indicate where additions or deletions have been made.

Wal-Mart owns a large commercial retail store built in 2000. It has 210,315 square feet of gross building area (GBA), which includes a greenhouse/garden center, and an auto care center. The 19.018 acre site is also improved with 590,000 square feet of paving. (Ex. 10).

Johnson County Assessor Tom Van Buer testified that sometime in 2016, Wal-Mart sold off a small portion of its site, reducing its site size to 18.97 acres for the 2016 assessment. Van Buer also testified about the market conditions in Johnson County, the assessment process, and a history of the subject property.

Based on sales that have occurred in Johnson County, Van Buer testified the general trend for commercial properties in Coralville indicates an increase in sale prices; and overall commercial vacancy rates have been less than 5%. He testified that the neighboring communities of North Liberty and Tiffin have seen historic growth. Van Buer explained while e-commerce could have an impact on the market of big-box retail stores like the subject, he has not seen this in his market.

Van Buer explained that while the income approach was developed by the Assessor's Office on the subject property, it was done as a check on the value of the property and not given weight in the assessment. He explained a 7.5% capitalization rate was applied in this analysis, which is the rate used on most retail properties in Johnson County. (Ex. 10, p. 7).

Van Buer explained a settlement was reached for the 2001-2002 assessment years and the subject property was assessed at \$13,300,000. (Ex. 10, p. 6). This assessment was unchanged until 2012. In 2013, the property was re-assessed for \$21,761,500; Wal-Mart petitioned this to the Board of Review, which reduced the value to \$18,134,600. Subsequently, Wal-Mart appealed to PAAB, and based on a stipulation between the parties the value was lowered to \$16,290,000, for the 2013 and 2014 assessment years. (Ex. 10, pp. 4 & 6).

Lastly, Van Buer notes that multiple permits were taken out between 2004 and 2011 to remodel the property. He explained this information helps the assessor determine the condition of the property and what depreciation may need to be applied.

The record includes three appraisals. Wal-Mart submitted two appraisals, one completed by Chris Jenkins, CBRE, West Des Moines, Iowa (Ex. 2); and the other by Dane Anderson, Situs RERC, West Des Moines, Iowa (Ex.1). Wal-Mart contends its two appraisals shift the burden of proof to the Board of Review. The Board of Review submitted an appraisal completed by Keith Westercamp, Appraisal Associates Company, Cedar Rapids, Iowa. (Ex. A). All of the appraisers are qualified to appraise the property and testified at hearing.

The following table summarizes the appraisers' approaches to value and their respective conclusions.

Appraiser	Sales Approach	Income Approach	Cost Approach	Final Opinion of Value
Jenkins	\$13,700,000	\$13,900,000	\$13,900,000	\$13,800,000
Anderson	\$11,600,000	\$12,195,000 ¹	\$12,195,000	\$11,600,000
Westercamp	\$16,710,000	\$16,185,000	\$19,200,000	\$17,300,000

*Anderson verbally modified these conclusions of his income and cost approaches at hearing.

A. Highest and Best Use

Jenkins concluded the subject property's highest and best use is "consistent with the existing use as a retail development." (Ex. 2, p. 59).

Anderson stated that "[g]iven the subject's current occupancy, achieved rents, and limited alternative uses, conversion of the existing improvements to an alternative use is not considered feasible." (Ex. 1, p. 46). Anderson concluded, "no altering of the improvements would appear to provide a higher return. . . . Therefore, the highest and best use, as improved, is considered continued single-tenant retail use. The most probable buyer is an owner occupant or speculative investor." (Ex. 1, p. 46).

Westercamp also found the highest and best use is its current use. (Ex. A, p. 56).

¹ Anderson verbally amended his report at the PAAB hearing, which modified his value indications by the income and cost approaches. He testified his modifications resulted in value indications of approximately \$11,900,000 in those approaches. Despite the descriptions of his modifications, PAAB was unable to replicate Anderson's conclusions. PAAB's calculations show a value by the income and cost approaches of \$12,195,000. The table above reflects PAAB's calculations.

B. Sales Comparison Approach

All of the appraisers identified the subject property as having a good location in retail corridor and in a prime commercial/retail area. (Ex. 1, p. 22, 67; Ex. 2, p. 10; Ex. A, p. 44, 56). Jenkins testified the subject's market area has strong occupancy for retail stores; however also testified that the subject's GBA was larger than most single-retail users require resulting in few potential users. Westercamp explained the subject is located in one of the most active markets in the Coralville area, and it continues to be a growth area.

1. *Jenkins Appraisal*

In describing his appraisal methodology for the subject, Jenkins indicated that "all three approaches have been utilized" but indicated the cost approach would be given minimal consideration. (Ex. 2, p. 48). Jenkins testified, "[t]he challenge is a lot of sales of retail stores are either sold as vacant or a long term leases, or they are build-to-suit that property." (Tr. p. 12, ln. 21-23). He claimed "The sales comparison approach is considered a reliable indication of value so that is given weight." (Tr. p. 39, ln. 16-18). But he also believed the income approach was reliable. (Tr. p. 39, ln. 18).

Jenkins admitted he could not find any sales in the subject property's corridor area due to the large size of the subject property and properties like the subject typically selling with a lease in place. (Tr. p. 68, ln.15 – p. 69, ln. 3). He stated, "the sales that do occur typically are not consistent with the requirements for fee simple valuation for assessment appeal purposes making it difficult to find appropriate comparable sales." (Ex. 2, p. 58).²

² The previous two paragraphs were not included in PAAB's 2017 Order.

Jenkins submitted seven sales he considered in his analysis, which are summarized in the following table. (Ex. 2, pp. 69-77).

Comp	Address	Sale Price	Sale Date	GBA	SP/GBA	Adjusted SP/GBA
J1	Burlington, IA	\$8,542,000	Apr-12	131,644	\$64.89	\$62.55
J2	Johnston, IA	\$5,900,000	Dec-14	146,003	\$40.41	\$50.92
J3	Ames, IA	\$3,650,000	Aug-15	60,053	\$60.78	\$60.76
J4	Port Huron, MI	\$9,796,179	Feb-13	193,590	\$50.60	\$64.36
J5	Rolling Meadows, IL	\$24,300,000	Jul-15	259,302	\$93.71	\$69.58
J6	Perry, GA	\$13,861,500	Jun-13	152,720	\$90.76	\$68.61
J7	York, SC	\$10,400,000	Nov-12	151,980	\$68.43	\$69.56

Jenkins testified that he searched regionally and nationally for sales of larger retail stores. In his opinion, size was a critical factor of comparison. The smallest sale he considered was roughly 60,000 square feet of GBA; the remainder of his sales ranged in GBA from approximately 131,500 to 260,000 square feet. Some of his sales were sold occupied and leased-fee. Others were sold vacant in fee simple, but Jenkins report admits “the price may be discounted in that situation.” (Ex. 2, p. 70). Jenkins made property rights adjustments to his leased sales, but it is unclear to PAAB how he determined the amount of his adjustments. The sales were also adjusted for market conditions (time), location, size, age/condition, and quality of construction. (Ex. 2, p. 74).

Sale J1 was a leased-fee sale located in Burlington. This sale had a long term lease when it sold, which Jenkins adjusted for in his analysis. He testified the 7.16% capitalization rate of this property reflects a long term lease to a good credit tenant. For this reason, he adjusted it downward in his analysis.

Sale J2 was an American TV & Appliance store in Johnston and was vacant at the time it sold. The property was a “dark store” meaning it was vacant at the time of sale. (Ex. 2, p. 71). Jenkins adjusted this property upward 20% to reflect its distressed sale. (Ex. 2, p. 74). Ultimately, Jenkins did not include this sale in his final sales comparison analysis.

Sale J3 is located in Ames and is Jenkins’ smallest comparable. It was vacant at the time it was purchased by Wal-Mart, and Jenkins asserts it was listed and marketed

as a retail store. Despite this, Wal-Mart purchased this property to tear down the existing improvements with the intent of expanding its existing store/operations located on an adjacent site.³ Jenkins did not adjust the sale for this factor. Regardless of the purchase price, PAAB finds this transaction represents a land sale not an improved sale. Moreover, because the purchaser was an adjoining land owner intent on expansion, the sale is considered abnormal thereby requiring either an adjustment to eliminate distortion of its market value or eliminating the sale from consideration. Iowa Code § 441.21(1)(b).

Sale J4 is a Super K-Mart located in Michigan, which had less than six years left on its lease. We note that when discussing his income approach to value, Jenkins recognized this property was occupied by a tenant with some financial difficulties and a shorter lease. PAAB assumes he is referring to the well-documented store closures and financial difficulties affecting Kmart. Accordingly, the capitalization rate from this sale was an outlier at 12.53%. Jenkins made no adjustment for the fact the property was leased to a poor-quality tenant.

Sale J5 is a Wal-Mart/Sam's Club in Illinois, located in the Chicago metro. These stores also had roughly five years left on their leases. This sale was partly vacant at the time of sale and the buyer was in discussions with the existing tenant, Wal-Mart, to extend its lease and accept a buyout of the retail space formerly occupied by Sam's Club. Further, the buyers intended to divide the Sam's Club space for multi-tenant use. (Ex. 2, p. 117-118). This sale was adjusted downward 25% for location.

Sale J6 is a Wal-Mart in Georgia with a lease in place. It sold in 2011 for \$10,700,000; the lease was subsequently extended and the property resold in 2013 for \$13,861,500. (Ex. 2, pp. 119-120). Jenkins explained this demonstrates the value of a longer lease so he adjusted for this factor. Jenkins acknowledged this sale is located in a smaller community compared to the subject's location. The Board of Review was critical of Jenkins for not making a location adjustment to this sale. In response, Jenkins

³ In the September 2017 PAAB Order this sentence stated: "Despite this, Wal-Mart, which owned the adjacent property, purchased this property to tear down the improvements and expand its existing store/operations. Jenkins did not adjust the sale for this factor."

admitted he did not document it in his report, but believes the population within a ten-mile radius of this property is similar to the subject's market area and supports his decision not to adjust for this factor.

Sale J7 is a Wal-Mart Super-Center in South Carolina with a lease in place. It sold in November 2012; the lease was subsequently extended and it resold in June 2013 for \$12,188,500. Jenkins, however, chose to rely on the 2012 sale of this property for his analysis. The Board of Review was also critical of the small 5% location adjustment to this sale, which Jenkins also acknowledged is in a much smaller population area than the subject property.

After adjustments, and excluding Sale 2, Jenkins' range of value was between \$60.76 and \$69.58. From within this range, he selected \$65.00 per square foot; or \$13,700,000 rounded. (Ex. 2, pp. 62-65).

2. Anderson Appraisal

In his sales comparison approach, Anderson indicated that "[i]n researching the market for big box transactions, limited data was located. A search of the local market for retail sales similar in size to the subject in the three years preceding the effective date yielded no transactions." (Ex. 1, p. 63). Thus, the scope of the sales search had to be expanded. (Ex. 1, p. 63).⁴

The following table is a summary of the seven Iowa, big-box stores that Anderson considered in his analysis. (Ex. 1, p. 65).

Comp	Address	Sale Price	Sale Date	GBA	SP/GBA	Adjusted SP/GBA
A1	Burlington, IA	\$9,662,000	Apr-12	133,894	\$72.16	\$63.79
A2	Fort Dodge, IA	\$3,800,000	Jan-15	87,272	43.54	\$48.33
A3	Sioux City, IA	\$3,015,200	Oct-11	87,762	\$34.36	\$43.04
A4	Cedar Falls, IA	\$8,050,000	Dec-12	88,064	\$91.41	\$79.25
A5	Cedar Rapids, IA	\$5,500,000	Mar-10	111,179	\$49.47	\$63.46*
A6	Davenport, IA	\$6,250,000	Dec-14	147,000	\$42.52	\$50.56*
A7	Johnston, IA	\$6,000,000	Dec-14	146,003	\$41.10	\$44.43*

*Anderson verbally modified the adjusted value of these sales at hearing.

⁴ This paragraph was not included in PAAB's 2017 Order.

Anderson acknowledged his search for comparable properties was focused on Iowa sales, and he was unable to find any single-tenant retail properties over 216,000 square feet of GBA. Anderson testified he was unable to find any sales larger than the subject property. He explained that while smaller properties are more expensive to build, they have a higher number of potential users making them more valuable than large properties like the subject. For this reason, all of the sales were adjusted downward for size.

He testified that with the exception of Sale A7, all of the sales were inferior in location compared to the subject property. He adjusted these sales between 10% and 35% for this factor. The location adjustments were based on the demographics of the purchasing power, population, lease rates, and traffic counts of the comparable locations compared to the subject property. (Ex. 1, pp. 68-69).

Sale A1 was a Lowes, which sold with a re-negotiated contract to update the property. This sale was also considered by Jenkins (J1); however, where Jenkins *subtracted* the tenant improvements and reported an adjusted sale price of \$8,542,000, Anderson *added* them to the sale price to arrive at an adjusted sale price of \$9,662,000.

Sale A2 was a multi-tenant property split between tenants Hobby Lobby and Marshalls. Anderson reported this sale as transferring in January 2015; however comments regarding the sale indicate it transferred in September 2011. (Ex. 1, p. 71 & 108). If the transfer date occurred in 2011, an upward adjustment for market conditions would be warranted.

Sale A3 was a former Wal-Mart located in Sioux City that was sold to Bomgaars. Despite the sale occurring in 2011 and Wal-Mart vacating the property, Bomgaars did not occupy it until after Wal-Mart's lease expired in January 2016. (Ex. 1, p. 109). Regardless of the fact the property had been physically vacant, Anderson identified it as 100% economically occupied because of the lease in place.

Sale A4 is a free-standing Kohl's located near the College Square Mall close to the University of Northern Iowa in Cedar Falls. It was significantly remodeled in 2011. The property was not actively marketed when it sold. (Ex. 1, p. 110).

Sale A5 was vacant at the time of sale and purchased by Theisen's, a regional home, farm, and auto retailer. Despite it being vacant when it sold, Anderson reported it as having 100% occupancy. (Ex. 1, p. 65). He acknowledged this was an error and it should have been reported at 0%. Anderson testified that this sale should have had an upward 10% year built (age)/condition adjustment, which would modify its adjusted value to \$63.46. Westercamp was critical of this sale, testifying that he had appraised the property several times. He explained it was originally built as an EconoFoods. Moreover, he noted there was a significant amount of on-going road construction projects, which coupled with its inferior location compared to the subject, impacted the desirability of this property. In his opinion, if it were to be used as a comparable to the subject, it would require significant location and condition adjustments.

Sale A6 is a 147,000 square foot free-standing retail store in Davenport. Anderson asserts this property was sold by an investor who had lost their tenant, which we presume was American TV & Appliance that went bankrupt. Anderson confirmed the sale with the listing Broker who would not label the sale as distressed, but admitted the seller "got what he could for the property." Anderson further acknowledged this property sold for roughly 20% less than its listing price. He believes an adjustment is debatable on this sale, but even if an upward 15% adjustment were made, it would not affect his final conclusions.

Sale A7 was another American TV and Appliance store, which sold to Goodwill Industries International, Inc. in December 2014. (Ex 1, p. 113). After issuing his report, Anderson later learned it sold from bankruptcy. Anderson noted it sold for 20% less than its list price with a shorter than typical marketing period. Anderson's interview with the Broker of this sale, suggested it sold for 15% less than market because of the distressed seller. For this reason, he admits it could be adjusted upward 15% in his analysis.

Anderson further adjusted Sales A1, A2, and A4 downward for "having long-term leases in place to credit tenants." (Ex. 1, p. 70). He made these adjustments, which range from 16% to 24%, by "comparing the actual capitalization rate to the estimated market capitalization rate, if leased to an average tenant with a typical retail lease term."

(Ex. 1, p. 70). It appears that his market capitalization rate used for this adjustment was the same as he derived in his income approach to value. The Board of Review was critical of Anderson asserting he did not determine if the leases were at or below market to justify his adjustment for this factor.

Anderson gave Sales A2, A5, A6, and A7 the most consideration in his sales comparison analysis because they required the least amount of adjustments. Despite applying additional adjustments to these sales at hearing, he asserts his final opinion of value is unchanged. These sales now have an adjusted range of \$44.43 to \$63.46, which he believes supports his original opinion of \$55.00 per square foot; or \$11,600,000 for the subject property.

3. Westercamp Appraisal

Westercamp testified that it was important to go beyond the sales comparison approach in this case. (Tr. p. 131, ln. 1-16). “Not a lot of sales that I was able to find in the state of Iowa.” (Tr. p. 144, ln. 21-22). His appraisal states, “[t]here are limited number of sales of newer style stores in a metro location in Iowa. Many Big Box Stores tend to have closely held ownership with the ownership related to the store.” (Ex. A, p. 98).⁵

The following table is a summary of the comparable properties that Westercamp considered in his analysis. (Ex. A, p. 86).

Comp	Address	Sale Price	Sale Date	GBA	SP/GBA	Adjusted SP/GBA
W1	Burlington, IA	\$8,887,000	Apr-12	131,644	\$67.51	\$81.11
W2	Omaha, NE	\$9,930,000	Jan-15	101,724	\$97.62	\$97.62
W3	Ankeny, IA	\$9,382,120	Dec-15	83,809	\$111.95	\$79.56

Westercamp testified that comparable sales were limited in the Coralville area. He explained his primary search was focused on larger properties located within Iowa. He acknowledged there were few sales available for analysis. All of Westercamp’s sales were occupied at the time they sold. In his opinion, vacant stores represent “second

⁵ This paragraph was not included in PAAB’s 2017 Order.

generation” space, which he identifies as typically older properties with different uses that may not meet the standards of the original use of the property.

Westercamp made minimal adjustments in his analysis; adjusting only for GBA, location, and quality. Wal-Mart was critical of the lack of adjustment for property rights.

Sale W1 is a Lowes in Burlington, Iowa that sold on lease-back, with a lease extended for ten years. In Westercamp’s opinion, Burlington is a weaker market than Coralville and therefore it was adjusted upward for location. Wal-Mart was critical of Westercamp for not making an adjustment to this sale because of its credit worthy tenant with a longer lease in place. Westercamp indicated that the “property rights are virtually the same for the subject and all cited conveyances” so he did not make any property rights adjustments. (Ex. A, p. 87).⁶ Moreover, Westercamp did not believe there was sufficient market support to make an adjustment for the differences in GBA between this sale and the subject.

Sale W2 is located in Omaha, Nebraska and was a car dealership. It is older than the subject property but renovated in 2007. Similar to Sale W1, Westercamp did not make a GBA adjustment to this sale, despite it being roughly half the size of the subject. Wal-Mart questioned whether this sale included the dealership business, however Westercamp reported it was his belief it did not include any business value. Wal-Mart also asserts this was a portfolio sale because Westercamp’s remarks on the sale indicated it involved two new car dealerships and a used car dealership.

Sale W3 was a HyVee located in Ankeny, Iowa. Although it is a smaller building, Westercamp believes it has similarities to a Wal-Mart as they both have grocery sales and some convenience items. In Westercamp’s opinion it offers a similar location, however Wal-Mart asserts it is a superior location with a higher surrounding population base. Wal-Mart further points out this was a leased-fee sale and its assessment was significantly less than its sales price; asserting the difference between the assessment and the sale price represents the investment value of the lease. We find Wal-Mart’s contention on this point to be speculative.

⁶ This sentence was not included in PAAB’s 2017 Order.

After adjustments, Westercamp's range of value was between \$79.56 and \$97.62. He gave most consideration to Sales W1 and W3, opining a value of \$82.06 per square foot; or \$16,710,000 rounded. (Ex. A, pp. 89-90).

C. Income Approach

Appraiser	Effective Gross Income (EGI)	Vacancy/Credit Loss	Operating Expenses	Net Operating Income (NOI)	Loaded Capitalization Rate	Total Value by Income Approach (rounded)
Jenkins	\$1,584,434	7%	(\$368,193)	\$1,216,242	8.74%	\$13,900,000
Anderson	\$2,008,424	8.7%	(\$952,727)	\$1,100,000	9.02%	\$12,195,000 ⁷
Westercamp	\$1,557,153	5%	(\$393,462)	\$1,163,691	7.19%	\$16,185,000

All of the appraisers concluded complimentary market rents between \$6.00 and \$7.00 per square foot, with Westercamp at the upper end of this range. Wal-Mart was critical of Westercamp for concluding a higher market rent of \$7.00 per square foot despite using all smaller properties with rents ranging from \$6.00 to \$6.75 per square foot. Typically rents go down as the building size increases.

Although Jenkins and Westercamp have divergent vacancy/credit loss estimates, they have similar EGI, Operating Expenses, and NOI estimates. Anderson's EGI is higher than both Jenkins and Westercamp, primarily because he included \$525,788 in real estate taxes as an operating expense. Anderson testified his operating income estimate was wrong due to the inclusion of real estate taxes within the expense reimbursement revenue. He asserts correcting for this error results in an NOI of roughly \$1,100,000. Ultimately, the appraisers conclude similar NOIs with an average of roughly \$1,150,000.

⁷ At the hearing, Anderson verbally modified his net operating income determination because his written report included real estate taxes as reimbursable expenses. He testified his modified opinion of value by the income approach is approximately \$11,900,000. Despite the descriptions of his modifications, PAAB was unable to replicate how Anderson arrived at his conclusion of \$11,900,000. PAAB's calculations show a value by the income approach of \$12,195,000 after removing the real estate taxes as a reimbursable expense. The table above reflects PAAB's calculations.

The primary distinction in their overall analysis comes down to the capitalization rate. Jenkins and Anderson determined a loaded capitalization rate of 8.74%, and 9.02% respectively. Westercamp determined a 7.19% loaded capitalization rate. This results in Westercamp's opinion of value being \$4,000,000 to \$5,000,000 higher than the other two appraisers.

Jenkins extracted capitalization rates of 7.16% and 6.06% from two of his comparable sales (Sales J1 and J6) that had long-term leases to credit tenants. He notes these rates are lower than market capitalization rates, which would consider an average quality tenant. (Ex. 2, p. 89). Jenkins relied on the capitalization rate of 8.04% for Sale 7; however, there was a more recent 2013 sale of this property, with an extended lease to Wal-Mart that Jenkins did not analyze. Jenkins explained the length of the lease impacts the capitalization rate; with longer leases typically having lower rates. Jenkins also testified that his Sale J4, which indicated a 12.53% capitalization rate, was occupied by a tenant with some financial difficulties and a shorter lease. In addition to extracting capitalization rates from the market, Jenkins spoke with a Real Estate Broker and considered published surveys and the band of investment.

Jenkins identified the subject as a Class B property when analyzing capitalization rates from surveys. (Ex. 2, p. 90). Jenkins explained the subject is located "in a good retail corridor with high traffic counts, but in a tertiary market..."

Jenkins selection of an 8.50% capitalization rate is exactly the same as the opinion of the single broker he interviewed and at the high end of the range of Class A or Class B properties from the CBRE Power Centers survey. (Ex. 2, p. 90). According to Jenkins' report, "the broker indicated a capitalization rate of around 8.50% would apply assuming a non-long term lease to a typical credit tenant." (Ex. 2, p. 91). Jenkins' report also details the broker's opinion that the subject property's most likely future use is for multi-tenant retail space. (Ex. 2, p. 90-91). This contrasts with Jenkins' evidence of three sales involving tenants with similar credit ratings as the subject property with capitalization rates between 6.06% and 8.04%, with a median of 7.16%. Despite this, Jenkins reconciled to an 8.74% loaded capitalization rate. (Ex. 2, p. 91-92).

Anderson extracted capitalization rates from Sales A1, A2, A3, and A4 in his sales comparison analysis, which ranged from 6.77% to 10.83%. (Ex. 1, p. 65). Sales A1 and A2 have extracted rates based on long-term, net leased property to a credit tenant of 6.77% to 7.60% respectively. (Ex. 1, pp. 85-86). Sale A3 has the highest extracted capitalization rate of 10.83%, as it was leased but not occupied with only four years left on its lease. Lastly, Sale A4 indicated a capitalization rate of 7.30% based on a build-to-suit agreement. Like Jenkins, Anderson acknowledges that because of “the long-term lease to a credit tenant the capitalization rate is significantly below a market capitalization rate, with a market rent, market lease term length, and *average quality* tenant.” (Emphasis added). (Ex. 1, p. 85).

In addition to the aforementioned sales, Anderson considered seven additional sales A-G from other markets with capitalization rates ranging from 6.15% to 10.25%. (Ex. 1, p. 86). The GBA of all of these sales was less than 20,000 square feet.

No specific information about these sales was included by Anderson to explain the differences within the range or for determining whether they are comparable properties.

In addition to extracting capitalization rates from the market, Anderson considered published surveys and the band of investment. His published surveys were based on “[s]econd-tier investment properties...defined as aging, former first-tier properties, in good to average locations.” (Ex. 1, p. 87).

Anderson selected an 8.75% capitalization rate despite his evidence of three credit-worthy tenant sales or built-to-suit properties. These sales are more akin to the current use of the subject property with capitalization rates ranging between 6.77% and 7.66% and a median of 7.30%.

Westercamp considered published surveys, the band of investment, and six Iowa sales in selecting a capitalization rate of 7%. His loaded capitalization rate is 7.19%. (Ex. A, pp. 79-80). Moreover, Westercamp testified the Iowa City metro area has historically had some of the lowest capitalization rates in Iowa. The GBA of the sales Westercamp relied on to extract capitalization rates, were all less than 32,000 square feet, with five of the sales having a GBA of 15,674 square feet or less. Like Anderson,

Westercamp did not include any specific information about these sales, such as age or the length of the remaining lease for PAAB to determine if they were comparable.

Cost Approach

The following table summarizes the appraisers' conclusions in their cost approaches.

Appraiser	Land Value	Replacement Cost New (RCN)	Total Depreciation	Total Value by Cost Approach (rounded)
Jenkins	\$7,850,000	\$16,377,000	(\$10,311,191)	\$13,900,000
Anderson	\$4,600,000	\$17,300,000	(\$9,705,000)	\$12,195,000 ⁸
Westercamp	\$7,450,000	\$15,712,532	(\$3,928,133)	\$19,200,000

All of the appraisers relied on MARSHALL AND SWIFT VALUATION SERVICE cost manual to estimate their replacement cost new (RCN). (Ex. 1, p 57; Ex. 2, p. 65; Ex. A, p. 62).

The appraisers concluded a range of site value between \$4,600,000 and \$7,850,000. Anderson was at the low end of this range, and roughly \$3,000,000 less than both Jenkins and Westercamp. Moreover, Anderson was significantly less than the January 1999 purchase price of the subject site, of roughly \$7,174,000. (Ex. A). Jenkins' land sales are among the most recent in the record. Anderson's land sales were recent, with only one located in Coralville and it was a 2010 transaction. Westercamp's land sales were the most similar in location to the subject property, but occurred between 2005 and 2010.

The appraisers had a tight range for the replacement cost new (RCN), but differed on the total depreciation, as noted in the table above.

All of the appraisers testified the subject property has a modern design and layout and does not suffer from functional obsolescence.

⁸ At the hearing, Anderson verbally modified his net operating income determination because his written report included real estate taxes as reimbursable expenses. This change also resulted in a modification to his economic obsolescence determination in his cost approach to value. Despite the descriptions of his modifications, PAAB was unable to replicate how Anderson arrived at his conclusion of \$11,900,000. PAAB's calculations show a value by the cost approach of \$12,195,000 after modifying the economic obsolescence. The table above reflects PAAB's calculations.

All relied on the economic age-life method to determine physical deterioration. (Ex. 1, p. 60; Ex. 2, p. 36; Ex. A, p.62). Jenkins concluded an age-life of 14/35 resulting in 40%, or \$6,550,800 physical deterioration. (Ex. 2, pp. 36, 68). Anderson concluded an age-life method of 10/40 resulting in 25%, or \$4,325,000 physical deterioration. (Ex. 1, p. 62). Westercamp concluded an age-life method of 10/35-40. (Ex. A, p. 48). He applied 25%, or \$3,928,133 physical depreciation.

Both Jenkins and Anderson assert the subject suffers from external obsolescence; whereas Westercamp does not believe this is the case – herein lies the distinction between the appraisers' cost conclusions.

Jenkins asserts there is external obsolescence to the subject property because there are very few users that would desire a building of this size for a single-occupant use, and because, in his opinion, it's in a smaller market. Using an income analysis comparing the cost feasible net operating income (NOI) to the stabilized NOI, Jenkins asserts the subject suffers from \$3,760,391 in external obsolescence; or 23% of the RCN. (Ex. 2, pp. 67-68). It is noted his cost feasible NOI is derived from the capitalization rate developed in his income approach to value. (Ex. 2, p. 67).

In Anderson's opinion, it is not economically feasible to build a speculative big-box retail building. Anderson applied external obsolescence based on a similar income feasibility analysis as Jenkins. (Ex. 1, p. 61). Applying his corrected NOI of \$1,100,000, he asserts the subject suffers from roughly \$5,380,000; or 31% of the RCN. After correcting his external obsolescence, his conclusion by the cost approach would be \$12,195,000.

Westercamp testified that the retail sales of a store are an important input in determining external obsolescence. He did not have this information available to him; however he has observed the subject on multiple occasions and in his opinion it is a busy store. Moreover, he believes more expansion of big-box stores is likely in the area. (Ex A. p. 56). Because the area has on-going, expanding development in a strong market area, he does not believe economic obsolescence exists.

Final Reconciliation

Although Jenkins developed the cost approach, he did not give it much consideration in his final reconciliation due to the large amount of depreciation considered. His appraisal indicates that both the sales and income approaches offer reliable indications of value. (Ex. 2, p. 94).⁹ He testified that he gave equal consideration to the sales and income approaches, concluding a value of \$13,800,000 for the subject property.

Despite modifying both his income and cost approach conclusions to \$12,195,000, Anderson asserts his final reconciled conclusion of \$11,600,000 is still reasonable and supported by the sales comparison approach.

Westercamp acknowledged that Iowa law prefers the sales comparison approach, however he gave all three approaches nearly equal consideration and arrived at a final opinion of value of \$17,300,000. (Ex. A, p. 100).

Analysis and Conclusions of Law

A. Burden Shifting

Wal-Mart asserts it shifted the burden of proof to the Board of Review, as provided under Iowa Code section 441.21(3)(b) (2015), by offering testimony and reports of two appraisers who opined the subject property is over assessed. The Board of Review, however, contends that neither of Wal-Mart's appraisers offered competent evidence of value and thus, did not shift the burden of proof.

Initially, the burden of proof in an assessment protest rests with the taxpayer, who "must establish a ground for protest by a preponderance of the evidence." *Compiano v. Bd. of Review of Polk Cnty.*, 771 N.W.2d 392.397 (Iowa 2009). However, if the taxpayer "offers competent evidence by at least two disinterested witnesses that the market value of the property is less than the market value determined by the assessor, the burden thereafter shall be upon the officials or persons seeking to uphold such valuation to be assessed." *Id.* at 396-97; § 441.21(3).

⁹ This sentence was not included in PAAB's 2017 Order.

Iowa law “requires the evidence offered by a disinterested witness to be competent before the burden of proof shifts to the board.” *Id.* at 398. “Evidence is competent under the statute when it complies ‘with the statutory scheme for property valuation for tax assessment purposes.’ ” *Id.* “[M]arket-value testimony by a taxpayer’s witness under a comparable-sales approach is ‘competent’ only if the properties upon which the witnesses based their opinions were comparable.” *Soifer v. Floyd Cnty. Bd. of Review*, 759 N.W.2d 775, 783 (Iowa 2009) (noting “If distorting sale factors or the points of difference between the assessed property and the other property are not quantifiable so as to permit the required adjustment, the other property will not be considered comparable.”); *Boekeloo v. Bd. of Review of City of Clinton*, 529 N.W.2d 275, 279 (Iowa 1995); *Bartlett & Co. Grain v. Floyd Cnty. Bd. of Review*, 253 N.W.2d 86, 88 (Iowa 1977). For the purposes of burden shifting, however, the *Soifer* Court also stated that “where the properties are reasonably similar, and a qualified expert states his opinion that they are sufficiently comparable for appraisal purposes, it is better to leave the dissimilarities to examination and cross-examination than to exclude the testimony altogether.” *Soifer*, 759 N.W.2d at 784. (quoting *Stewart v. Commonwealth*, 337 S.W.2d 880, 884 (Ky. Ct. App. 1960)). If the sale properties “are comparable, the two witnesses’ opinions constitute ‘competent evidence’ and the burden of persuasion” shifts, “otherwise it does not shift.” *Bartlett & Co. Grain*, 253 N.W.2d at 88; *Soifer*, 759 N.W.2d at 783. Nonetheless, “the mere fact that sales might be considered comparable . . . does not necessarily mean that valuation based on them is credible.” *Wellmark, Inc. v. Polk Cnty. Bd. of Review*, 875 N.W.2d 667, 682 (Iowa 2016) (citing *Soifer*, 759 N.W.2d at 784).

PAAB finds Wal-Mart provided two disinterested witnesses, Jenkins and Anderson, who were lawfully competent to testify. Jenkins and Anderson concluded the market value of the subject property is less than its assessed value. Both offered evidence complying with the statutory scheme for real estate valuation by initially conducting the sales comparison approach to value whereby sufficiently comparable properties were considered and adjusted. They also considered other appraisal methods as provided in Iowa Code section 441.21(2).

Here we find Jenkins and Anderson both provided competent evidence of the property's market value and thereby shifted the burden of proof to the Board of Review.

B. Subject Property's Actual or Fair Market Value

Wal-Mart argues the subject property is assessed for more than its market value, as provided under Iowa Code section 441.37(1)(a)(1)(b) (2015). PAAB "makes its independent determination of the value based on all the evidence." *Compiano*, 771 N.W.2d at 397. "Ultimately, the burden of proof is one of persuasion" which "comes into play after all of the evidence is introduced at hearing." *Id.* at 397 n.3. All evidence is to be considered. Iowa Code § 441.37A(3)(a).

In Iowa, property is assessed for taxation purposes following Iowa Code section 441.21. Iowa Code subsections 441.21(1)(a-b) require property subject to taxation to be assessed at its actual value, or fair market value. *Soifer*, 759 N.W.2d at 778.

"*Market value*" is defined as the fair and reasonable exchange in the year in which the property is listed and valued between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and each being familiar with all the facts relating to the particular property.

§ 441.21(1)(b).

In determining market value, "[s]ales prices of the property or comparable property in normal transactions reflecting market value, and the probable availability or unavailability of persons interested in purchasing the property, shall be taken into consideration in arriving at market value." *Id.* Using the sales price of the property, or sales of comparable properties, is the preferred method of valuing real property in Iowa. *Id.*; *Compiano*, 771 N.W.2d at 398; *Soifer*, 759 N.W.2d at 779 n. 2; *Heritage Cablevision v. Bd. of Review of Mason City*, 457 N.W.2d 594, 597 (Iowa 1990). "[A]bnormal transactions not reflecting market value shall not be taken into account, or shall be adjusted to eliminate the effect of factors which distort market value"

§ 441.21(1)(b). Abnormal transactions include, but are not limited to, foreclosure or other forced sales, contract sales, discounted purchase transactions, or purchases of adjoining land or other land to be operated as a unit. *Id.*

The first step in this process is determining if *comparable* sales exist. *Soifer*, 759 N.W.2d at 783. If PAAB is not persuaded as to the comparability of the properties, then it “cannot consider the sales prices of those” properties. *Id.* at 782 (citing *Bartlett & Co. Grain Co. v. Bd. of Review of Sioux City*, 253 N.W.2d 86, 88 (Iowa 1977)). “Whether other property is sufficiently similar and its sale sufficiently normal to be considered on the question of value is left to the sound discretion of the trial court.” *Id.* at 783 (citing *Bartlett & Co. Grain*, 253 N.W.2d at 94).

Similar does not mean identical and properties may be considered similar even if they possess various points of difference. *Id.* (other citations omitted). “Factors that bear on the competency of evidence of other sales include, with respect to the property, its ‘[s]ize, use, location and character,’ and, with respect to the sale, its nature and timing. *Id.* (other citations omitted). Sales prices must be adjusted “to account for differences between the comparable property and the assessed property to the extent any differences would distort the market value of the assessed property in the absence of such adjustments”. *Id.* (other citations omitted). “[A] difference in use does affect the persuasiveness of such evidence because ‘as differences increase the weight to be given to the sale price of the other property must of course be correspondingly reduced.’” *Soifer*, 759 N.W.2d at 785 (quoting *Bartlett & Co. Grain*, 253 N.W.2d at 93).

“The burden of persuasion rests on the party seeking to show that market data cannot readily establish market value before proceeding to the other-factors approach to valuation.” *Wellmark, Inc. v. Polk Cnty. Bd. of Review*, 875 N.W.2d 667, 682 (Iowa 2016). Where a party bearing the burden convinces PAAB that comparable sales do not exist or cannot *readily* determine market value, then other factors may be used. § 441.21(1)(b); *Compiano*, 771 N.W.2d at 398 (citing *Soifer*, 759 N.W.2d at 782); *Carlton Co. v. Bd. of Review of City of Clinton*, 572 N.W.2d 146, 150 (Iowa 1997); § 441.21(2). If sales cannot readily establish market value, “then the assessor may determine the value of the property using the other uniform and recognized appraisal methods,” such as income and/or cost. § 441.21(2).

[A]ssessors are permitted to consider the use of property as a going concern in its valuation. *Riso v. Pottawattamie Cnty. Bd. of Review*, 362 N.W.2d 513, 517 (Iowa

1985). In *Maytag Co. v. Partridge*, 210 N.W.2d 584 (Iowa 1973), an expert opined that the assessed value of Maytag's machinery should be based on its secondary resale value. The Iowa Supreme Court rejected that approach, noting "the rule is that an assessor must also consider conditions existing at the time and the condition of the property in which the owner holds it." *Id.* at 589. When an assessor values property as a going concern, "he is merely following the rule that he must consider conditions as they are." *Soifer*, 759 N.W.2d at 788 (quoting *Maytag Co. v. Partridge*, 210 N.W.2d 584, 590 (Iowa 1973)). The assessor is "recognizing the effect of the use upon the value of the property itself. He is not adding on separate items for good will, patents, or personnel." *Id.*

The Iowa Supreme Court recently reaffirmed this principle in *Wellmark, Inc. v. Polk County Board of Review*. 875 N.W.2d at 670-71. In that case, Wellmark's experts valued the single-occupant corporate headquarters "by using an analysis of multitenant office buildings," reasoning that a purchaser would likely convert the property to a multitenant use. *Id.* at 671. In evaluating the theories of value-in-use and value-in-exchange pertaining to Wellmark's property, the Iowa Supreme Court adopted the view that "value should be based on the presumed existence of a hypothetical buyer at its current use." *Id.* at 683. The Court rejected Wellmark's experts' opinions valuing the property as a multitenant office building and, instead, concluded the property should be valued based on its current use as a single-occupant office building. *Id.* at 682-83.

"[T]he proper measure of the value of property is what the property would bring if sold in fee simple, free and clear of any leases." *I.C.M. Realty v. Woodward*, 433 N.W.2d 760, 762 (Iowa Ct. App. 1988) (emphasis added); *Merle Hay Mall v. City of Des Moines Board of Review*, 564 N.W.2d 419 (Iowa 1997); *Oberstein v. Adair Cnty. Bd. of Review*, 318 N.W.2d 817 (Iowa Ct. App. 1982). The Iowa courts have repeatedly held that unfavorable leases should not be used to lower assessments. *Merle Hay Mall*, 564 N.W.2d 419 (holding that an unfavorable lease does not reduce a property's assessed value); *Oberstein*, 318 N.W.2d at 819.

Sales Comparison Approach

In its Ruling, the District Court concluded “PAAB erred in concluding that comparable sales data were not available or readily ascertainable without first requiring that Johnson County prove as much by a preponderance of the evidence.” (D. Ct. Ruling p. 6). We note it appears the District Court may have erroneously conflated the burden shifting provision in section 441.21(3) and the question of whether comparable sales data can readily establish value under section 441.21(2).

In hindsight, however, we agree that our first Order did not accurately describe the legal standard that must be met prior to moving to other factors under Iowa Code section 441.21(2). This does not mean, however, that the standard was not met.¹⁰

In *Wellmark*, the Court noted “a party cannot move to other-factors valuation unless a showing is made that market value of the property cannot be readily established through market transactions.” 875 N.W.2d at 682. The Court then examined this question. *Id.* Similar to this case, in *Wellmark* the ultimate burden of proof had shifted to the Board of Review pursuant to section 441.21(3). *Id.* at 671. Nevertheless, the Court examined *Wellmark*’s evidence and the Board of Review’s evidence to conclude *Wellmark*’s value could not readily be established through a comparable sales analysis. *Id.* at 682. It noted that *Wellmark*’s experts used “office buildings dedicated to multitenant use”, in contrast to that property’s single-occupant use, and had to make substantial adjustments to their sales to support their analysis. *Id.* The Board of Review’s expert used large office buildings like *Wellmark*’s property but from much larger metropolitan areas than Des Moines. *Id.* It also noted some of his comparables also included properties sold subject to long-term leases. *Id.* In sum, the Court concluded “the district court correctly considered other factors in its effort to establish the value of the properties.” *Id.*

Following the framework set forth in *Wellmark*, we consider all of the evidence in determining whether the Board of Review has met its burden of showing that the sales

¹⁰ Notably, the District Court did not engage in a substantial evidence analysis regarding this question. Thus, the question as to whether the standard has been met is a matter for PAAB to now consider.

comparison approach cannot readily establish the market value of Wal-Mart's property and that other factors should be considered under section 441.21(2).¹¹

With this in mind, we reiterate the substantial evidence offered from both parties that properties like the subject are not often sold in fee-simple for continued use by a single tenant. They indicated difficulty in finding comparable sales, which necessitated expanding the scope of their sales search. These are similar to the considerations that caused the *Wellmark* Court to turn to the other-factors approach. *Id.*

Further, the Board of Review's appraiser and one of Wal-Mart's appraisers were not willing to give full weight to the sales comparison approach in their reconciliation. The only appraiser willing to give the sales comparison approach the most weight is also the appraiser PAAB finds the least credible. Because of the appraisers' expressed opinions about the limited reliability of the sales comparison approaches and the defects we find in their approaches, we conclude the Board of Review has established by a preponderance of the evidence that the subject's market value cannot be readily established by the sales comparison approach alone.¹² See *Wellmark*, 875 N.W.2d at 672; *Carlton*, 572 N.W.2d at 149-50 (noting party relying on "other factors" approach has the burden of persuading factfinder that property's fair market value cannot be readily established by the sales comparison approach); *Equitable Life Ins. Co. v. Bd. of Review of City of Des Moines*, 281 N.W.2d 821, 825 (Iowa 1979) (Court adopted assumption that the evidence implicitly indicated the property's market value could not be readily established by sales comparison approach alone and gave consideration to all three appraisal methods).

A review of the sales used by the appraisers bolsters this conclusion. All of the appraisers relied on sales of significantly smaller properties, or properties located in

¹¹ This is also in line with the statutory mandate that PAAB "consider all of the evidence." § 441.37A(3)(a).

¹² "The sales prices approach depends on the availability of the sales price of the property or comparable property in normal transactions." *Equitable Life Ins. Co.*, 281 N.W.2d at 823. Certain determinations regarding the sales comparison approach are within the realm of the factfinder, in this case PAAB. "Whether other property is sufficiently similar and its sale sufficiently normal to be considered on the question of value is left to the sound discretion of the trial court." *Soifer*, 759 N.W.2d at 783. Notwithstanding the language of section 441.21, in light of the deference given to the factfinder to determine whether specific sales should be considered, it stands to reason the factfinder should also be given some deference in determining whether the sales comparison approach can readily establish value in a particular case, after having considered all of the testimony and evidence.

inferior areas with less appeal compared to the subject's location. Jenkins and Anderson relied on sales we find were distressed (J2, A6, and A7). Jenkins made an adjustment for this factor in his original analysis. Anderson orally modified his analysis to include adjustments for this factor. Jenkins testified Sale J4 was occupied by a tenant with some financial difficulties and a shorter lease. The sale has the highest capitalization rate of any of Jenkins' sales at 12.53%, indicating the increased risk involved with this purchase. We are not inclined to place any reliance on these sales.

Jenkins also included the sale of a property purchased by the adjoining land owner with the intent of demolishing the improvements and expanding its operations (J3). PAAB believes this transaction better represents a land sale than an improved sale. Without adjustment, this sale may not be considered, as provided under Iowa Code section 441.21(1).

They also relied on sales that were vacant at the time they sold (A5 and J5). We find the fact the properties were vacant does not render them *per se* unreliable, but vacant properties require special care as other attributes of the sale may necessitate additional research and adjustment. In the case of Sale A5, we are not inclined to give it any weight because it is a dated sale and the property's use changed after purchase. Testimony indicated significant remodeling took place after purchase and Anderson failed to adjust for that fact. APPRAISAL INSTITUTE, THE APPRAISAL OF REAL ESTATE 412 (14th ed. 2013).¹³ ¹⁴ Sale J5 was partly vacant at the time of sale and the buyer was in discussions with the existing tenant, Wal-Mart, to extend its lease and accept a buyout of the retail space formerly occupied by Sam's Club. Further, the buyers intended to divide the Sam's Club space for multi-tenant use.

Jenkins made a downward adjustment for expenditures made after the purchase of J1, despite the fact that post-sale capital expenditures normally require a positive

¹³ THE APPRAISAL OF REAL ESTATE (14th ed.) is a commonly cited appraisal text published by the Appraisal Institute.

¹⁴ "A knowledgeable buyer considers expenditures that will have to be made upon purchase of a property because those costs affect the price the buyer agrees to pay." THE APPRAISAL OF REAL ESTATE 412. These expenditures can include, but are not limited to, costs to demolish and remove a portion of the improvements, and costs for additions or improvements to the property. *Id.* "The relevant figure is not the actual cost that was incurred but the cost that was *anticipated* by both the buyer and seller." *Id.* (emphasis added).

adjustment. *Id.* In considering the same sale (A1), Anderson made a positive adjustment.

Considering the foregoing, we give no weight to Jenkins Sales J1, J2, J3, and J4. His remaining sales have an adjusted range from \$68.61 to \$69.58 per-square-foot. Accordingly, we find Jenkins' reconciled value of \$65.00 per-square-foot is too low.

Of Anderson's remaining sales, he also included a multi-tenant property (A2), which PAAB does not consider similar to the subject's single-occupant use. While A2 has net adjustments of 11%, Anderson made gross adjustments totaling 62%; indicating the property lacks comparability with the subject. While we are willing to give consideration to Anderson's remaining sales (A1, A3, and A4), we also generally find them inferior to the subject. In our view, Anderson's selection of inferior comparables in his sales approach caused an undervaluation of the subject property. *See id.* at 404 (recognizing the importance of bracketing). Moreover Sales A1, A3, and A4 have an adjusted range from \$43.04 to \$79.25 per-square-foot with an average of \$62.03 and a median of \$63.79; further demonstrating Anderson's reconciled value of \$55.00 per-square-foot is too low.

Westercamp submitted only three comparable properties in his analysis, but unlike Jenkins' and Anderson's sales they were all occupied when they sold demonstrating continued and on-going occupant retail use pre- and post-sale. Iowa Courts have found properties with continued use to be more persuasive than properties that changed use after the sale. *Soifer*, 59 N.W.2d at 784-89; *Hy-Vee, Inc. v. Dallas County Bd. of Review*, 2014 WL 4937892 at *5 (Iowa Ct. App. Oct. 1, 2014). In Westercamp's opinion, it is not reasonable to compare vacant stores or bankruptcy sales to the subject property.

Wal-Mart was critical of Westercamp for relying on what it believed was a portfolio sale (Sale W2). Westercamp's analysis of Sale W2 resulted in no adjustments, despite having roughly 50% less GBA than the subject. Nonetheless, he gave this sale the least consideration in his analysis. (Ex. A, p. 90). Because of these issues, we would not give it any weight.

Westercamp's remaining sales have adjusted sales prices of \$79.56 (W3) and \$81.11 (W1). Wal-Mart criticizes the lack of property rights adjustments on these sales. However, the District Court's ruling, and its consideration of the special use prohibition in Iowa Code section 441.21(2), suggests that Wal-Mart's criticism may lack all merit.

In determining whether the sales comparison approach could readily establish value in *Wellmark*, the Iowa Supreme Court recognized that one of the Board of Review's experts relied on some comparable properties sold subject to long term leases. 875 N.W.2d at 682. The Court stated this fact "cloud[ed] comparability and rais[es] the question of whether the buyer was interested in the property or the income stream generated by an advantageous lease." *Id.* The Court then concluded the district court properly considered other factors in valuing the property. *Id.*

THE APPRAISAL OF REAL ESTATE indicates that "[i]f the sale of a leased property is to be used as a comparable sale in the valuation of the fee simple estate of another property, the comparable sale can only be used if reasonable and supported market adjustments for the differences in rights can be made." APPRAISAL INSTITUTE, THE APPRAISAL OF REAL ESTATE 406 (14th ed. 2013). It gives the following example:

For example, consider the appraisal of the fee simple estate in real estate that is improved with an office building. A similar improved property was fully leased at the time of sale, the leases were long-term, and the credit rating of the tenants were good. To compare this leased fee interest to the fee simple estate of the subject property, the appraiser must determine if the contract rent of the comparable property was above, below, or equal to market rent. [] If the market rent for office space is \$25 per square foot net and the average contract rent for the comparable property is \$20 per square foot net, then the difference between market and contract rent is \$5 per square foot.

"In comparing properties that are encumbered by long-term leases or are essentially fully leased with quality tenants, the appraiser must recognize that these leased properties may have significantly less risk than a competitive property that has shorter-term tenants at market rental rates." *Id.* at 407. However, "the reverse may be true in expanding markets" where sufficient tenants are available for shorter-term leases at higher rental rates. *Id.*

THE APPRAISAL OF REAL ESTATE notes the challenges with making adjustments for property rights. “Calculations of appropriate adjustments reflecting differences in property rights may be difficult to develop and support. Properly developed adjustments require significant research and diligence.” *Id.* at 407. At the same time, it notes the cost approach “produces a value indication of the fee simple estate of a property at market rent and stabilized occupancy.” *Id.* at 638. Similarly, when the fee simple interest of a property is valued using the income capitalization approach, “the presumption is that the property is available to be leased at market rates.” *Id.* at 441. Thus, there may be some wisdom in giving consideration to the other valuation approaches where there is a question of whether the adjusted sales fairly reflect the fee simple value sought by Iowa law.

In considering a retail store subject to a below market lease in *Foreman & Clark of Iowa, Inc. v. Bd. of Review of City of Cedar Rapids*, the Iowa Supreme Court concluded “the effect of the lease must be considered as a factor in determining adjustments to the contract sales price.” 286 N.W.2d 169, 173 (Iowa 1979). The Court adjusted the sale “by considering the economic terms of the existing lease.” *Id.* The Court went on to note that other matters must be considered regarding adjustments. *Id.* The Court referenced testimony indicating “commercial property is usually purchased subject to a lease.” It stated, “[t]he fact the premises had a lease, guaranteeing a reasonable income for several years, has to be weighed as a positive factor” against evidence of the negative impacts of a new mall and new retail space. *Id.* Ultimately, the Court found no error in the assessment, despite the failure to consider “the effect of the lease on the sale price . . . when weighing whether the contract sale price should be adjusted upward, downward, or left undisturbed in determining the property’s market value.” *Id.*

Ultimately, in adjusting sales subject to leases, we believe the appraiser should make any necessary adjustments to estimate the market value of the subject property consistent with section 441.21(1). This task may involve consideration of the subject’s market earning capacity as identified in section 441.21(2) and could require making positive, negative, or no adjustments, as the situation may dictate. Adapting a frame of

analysis from *Wellmark*, the valuation, and the adjustments made to arrive at that valuation, should be based on the presumed existence of a hypothetical renter at its current use. *Wellmark*, 875 N.W.2d at 683 (adopting the view that the value of Wellmark’s single tenant corporate headquarters should be “based on the presumed existence of a hypothetical buyer at its current use.”).

Based on our experience and the foregoing case law, the appraiser should consider whether adjustments to comparable sales that sold subject to a lease are necessary, but must not always make an adjustment. Westercamp’s appraisal explains why he did not make a property rights adjustment.¹⁵ (Ex. A, p. 87). He believed that “property rights are virtually same for the subject and all cited conveyances. No lease adversely impairs value.” (Ex. A, p. 87). This is consistent with the above cited case law and *Merle Hay Mall*, 564 N.W.2d at 422. Thus, we find no error.

PAAB finds Jenkins’ and Anderson’s use of sales that were distressed, vacant stores or in areas significantly inferior to the subject’s location resulted in artificially low conclusions. They were not valuing the current use of the subject property as a single-occupant retail space in a prime location. In support of its position, Wal-Mart notes Jenkins and Anderson adjusted their leased-fee sales for the property rights associated with the sales. We do not believe the use of an adjustment such as this can remedy the fact that the majority of the sales should not have been relied in the first place. Further, PAAB notes that Anderson’s adjustment appears to be based off of the capitalization rate he determined in his income approach to value, which we find is too high. Conversely, the record is not clear as to how Jenkins arrived at his property rights adjustments.

As noted previously in this Order and in the District Court ruling, the Board of Review bears the burden of showing the comparable sales approach cannot readily establish the value in order to use other approaches to value. We have detailed our concerns about the quality of the sales the appraisers utilized in the preceding paragraphs. Many of the sales on which the appraisers rely are identified as abnormal

¹⁵ We note our prior order wrongly stated that Westercamp did not consider property rights adjustments. While he did not make property rights adjustments, his appraisal indicates he evaluated the sales to determine whether adjustments should be made.

sales under section 441.21(1). In fairness to the sales comparison approach usage requirement in section 441.21(1), we do not think it is sensible to only rely upon that approach when the majority of sales in the record are found to be abnormal sales under the same code section. Hypersensitivity to the sales comparison approach requirement should not be viewed as permission to utilize sales that violate statutory directives.

Aside from that, we again note that all of the appraisers testified to difficulty finding comparable sales. Only Anderson, whose appraisal we find least persuasive, placed full reliance on the sales comparison approach in reconciling to his final value opinion. Jenkins testified he gave weight to all three approaches, with greater weight to sales and income. Westercamp gave 30% weight each to the cost and income approaches and 40% weight to the sales comparison approach. Based on the entirety of the record, we believe substantial evidence shows the Board of Review has met its burden that the sales comparison approach alone cannot establish the subject property's value.

Even if we would be limited to considering only the sales comparison approaches offered by the appraisers, despite their own reticence to fully rely upon them, we believe Westercamp offered the most persuasive sales comparison approach. We find Westercamp's use of properties with on-going retail occupancy more persuasive than the distressed, inferior property sales utilized by Wal-Mart's experts.

Income Approach

All of the appraisers concluded complimentary rents between \$6.00 and \$7.00 per square foot; and all conclude similar NOI's with an average of roughly \$1,150,000. The distinction in their income analysis comes down to the capitalization rate. Jenkins and Anderson determined a loaded capitalization rate of 8.74%, and 9.02% respectively. Westercamp determined a 7.19% loaded capitalization rate. This results in Westercamp's opinion of value being \$4,000,000 to \$5,000,000 higher than the other two appraisers.

Both Jenkins and Anderson included extracted capitalization rates of investment grade quality properties, like the subject, that ranged between 6.06% and 7.66% (Sales

J1, J6, A1, and A2). We previously found Sales A1 and A2 were inferior to the subject, yet Anderson's capitalization rate is well-above the capitalization rate indicated by these sales.

Anderson also examined other retail property sales in Iowa in determining his capitalization rate (Sales A-G). (Ex. 1, p. 86). There is very little information about these properties in the record, but we note Sales C and G appear to be outliers and, in our view, should not have been considered. Nonetheless, despite considering those sales, Anderson's capitalization rate of 8.50% is greater than the average (8.31%).

Anderson also reviewed investor surveys for second-tier investment properties in the Midwest. (Ex. 1, p. 87). Anderson asserts it is appropriate to compare the subject property to "second-tier investment properties...defined as aging, former first-tier properties, in good to average locations." (Ex. 1, p. 87). PAAB notes the assessed value of a property is required to reflect the value of the property in its current use.

Jenkins also considered five of his sales in determining his capitalization rate. (Ex. 2, p. 89). We previously found we were not going to consider Sale J1 in the sales comparison approach, and we likewise decline to consider it here. Sale J4 also appears to be a significant outlier and we give it no consideration. The remaining three sales indicate a range from 6.06% to 9.54%. We note Sale J5, which sets the upper limit of the range, had increased risk due to the actual vacancy of the Sam's Club retail space. All else being equal, this would have caused an elevated capitalization rate.

Like Anderson, Jenkins also considered investor surveys. (Ex. 2, p. 90). In his opinion, the subject is a Class B property, which indicated a range of 6.50% to 10% with an average of 7.76%. Jenkins chose the upper portion of this range because he considered the subject to be in a tertiary market.

Jenkins also spoke to a local broker who indicated a capitalization rate around 8.50%, assuming a non-long term lease to a typical credit tenant. (Ex. 2, p. 78-79). In reviewing Jenkins' report, the broker was of the opinion the most probable future use of the subject is to be converted into a multi-tenant space. We note this is not the current use of the subject and modifies the risk determination that impacts the capitalization

rate. In any event, Jenkins' loaded capitalization rate slightly exceeds the broker's opinion.

Westercamp concluded a lower loaded capitalization rate of 7.19%. (Ex. A, p. 80). He relied on the band of investment, as well as market comparables and investor surveys, in arriving at his conclusion. However, the sales he analyzed were, on average, 20-times smaller than the subject. Further, PAAB finds Westercamp provided insufficient evidence to support his capitalization rate.

The capitalization rate is a function of risk and the ability of the real estate to provide a return on and a return of capital. As of the date of assessment, the subject is a retail property occupied by a single user, located in a good retail corridor. The evidence in the record indicates increased retail construction and low vacancy rates. Given these characteristics, if vacant, PAAB believes the subject property would generate significant demand by similar or nearly similar occupants in quality as its current occupant. Thus, the risk of this property not being able to provide an adequate return on and of capital is relatively low.

As expressed by their capitalization rates, we find Anderson and Jenkins overestimated the risk associated with the subject property. This appears to be based, in part, on a perceived lack of potential buyers of the subject property for single-occupant use sometime in the future. Their judgments regarding the property's future use enhance its risk, thereby increasing the capitalization rate, and reducing their value conclusions. Because of the demographics of the subject property's surrounding market, we do not believe those judgments are true to the facts.

Moreover, our analysis of the evidence indicates their selected capitalization rates are not supported by the data. Both appraisers had evidence of lower capitalization rates that better reflect the current use of the subject property and indicate the loaded capitalization rates they selected is excessive.

PAAB finds Westercamp's capitalization rate unreliable because he relied on sales that were 20-times smaller than the subject. Despite this, his capitalization rate of 7.00% is aligned with Jenkins and Anderson's evidence that suggests a capitalization rate between 6.06% and 7.66%.

We note both Jenkins and Anderson also used their higher capitalization rates in various capacities in their sales comparison approach and cost approach. This overestimation of the capitalization rate makes their conclusions under those approaches suspect as well.

Cost Approach

Both Jenkins and Anderson assert the subject suffers from external obsolescence in the cost approach, despite recognizing there is low vacancy and no indication of depressed rents. This distinguishes their conclusions from Westercamp's. Both used the same methodology to determine the amount of external obsolescence they assert exists, which relies on the extracted capitalization rate from their income approaches as a key factor in the formula. Moreover, PAAB recognizes that if the capitalization rate is incorrect, it would affect the conclusions. Here, PAAB finds the capitalization rates relied on by Jenkins and Anderson are too high. Thus, using the capitalization rates in their cost approach, Jenkins and Anderson have overestimated external obsolescence. This artificially reduces their conclusion by the cost approach.

Additionally, we find Anderson's opinion of the site value to be an outlier in the record. Both Jenkins and Westercamp arrive at similar site values which we find more closely resemble the subject's land value.

Westercamp does not believe the subject property has any external obsolescence, which is typically identified in the market by higher vacancy and lower rents. The record is clear the subject is in a good retail corridor, with low vacancy and no indication that rents are lagging.

Further, PAAB finds the record supports a capitalization rate of between 6.06% and 7.66%. The lower capitalization rate range results in less than \$500,000 income loss; or less than 0.031% obsolescence. Thus, we find Jenkins and Anderson overestimate the property's economic obsolescence.

C. Conclusion

In its Ruling, the District Court found that PAAB erred in its prior order by giving Jenkins and Westercamp equal weight and thereby modifying the assessment to a value in between the two appraisals. The Court stated, “[PAAB] should have either decided which expert analysis to rely on in coming to a final conclusion or found that Johnson County had failed to carry its burden.” (D. Ct. Ruling p. 9). It found PAAB used a decision making process prohibited by law. (D. Ct. Ruling p. 9) (citing Iowa Code § 17.19(10)(d)).

As asserted in a Rule 1.904 Motion to Reconsider, PAAB believes the Court’s conclusion rests on an erroneous reading of *Heritage Cablevision v. Bd. of Review of Mason City*, 457 N.W.2d 594 (Iowa 1990). In its Ruling on that Motion, the District Court wrongly placed a burden on PAAB to demonstrate that its method was not prohibited by law. (D. Ct. Ruling p. 9). In a judicial review proceeding, the petitioner bears the burden of establishing the agency’s action is erroneous. § 17A.19(8).¹⁶ Moreover, the District Court cited no case law or statutory law that specifically prohibits PAAB’s method.

In *Wellmark*, the Iowa Supreme Court detailed a Maryland case where the trial court gave weight to multiple appraisers’ opinions in arriving at value conclusion. 875 N.W.2d at 677-78. The Court then stated, “The approach of the trial court seems somewhat undisciplined, but perhaps its candor should be applauded for avoiding exaggerated claims of certainty and recognizing that valuation is, at best, an educated guess.” *Id.*

Like the Maryland court cited in *Wellmark*, PAAB does not believe any of the appraisals offer an indisputably reliable opinion of value for the subject property and therefore PAAB weighed them in a fashion consistent with our opinion about their reliability. There is no statutory prohibition against the approach PAAB utilized and language in *Compiano* seems to support it. “[I]f the court determines the grounds of

¹⁶ We note that in the judicial review proceeding, Wal-Mart did not specifically argue in either its brief or reply brief that PAAB utilized a decision making process that was prohibited by law. In fact, in listing its claims under section 17A.19(10) in its brief, Wal-Mart did not identify a claim under section 17A.19(10)(d). (Wal-Mart D. Ct. Brf. p. 5). Moreover, neither party cited the *Heritage* case on which the District Court relied. As such, we believe the Court’s conclusion on this matter is legal error.

protest have been established, it must then determine the value or correct assessment of the property. . . Here, the court makes its independent determination of the value based on all the evidence.” 711 N.W.2d at 397. We believe the District Court’s conclusion is erroneous.

Despite our misgivings about the District Court’s conclusion on this question, we are bound to follow it. Accordingly, we now consider whether the Board of Review has upheld its burden to support the assessment.

Wal-Mart’s appraisers (Anderson and Jenkins) both had lower conclusions of value within their different approaches to value based primarily on the selection of their comparable properties, capitalization rates, and application of external obsolescence. We find Jenkins and Anderson overestimated the risk associated with the subject property, relied on inferior sales, their conclusions did not reflect the property’s current use, and the most reliable evidence does not support their capitalization rates.

PAAB further concludes Anderson’s appraisal is not only the least reliable in the record, but not a credible indication of the property’s value. Anderson had to orally amend his report at hearing due to errors. Despite the fact his corrections increased his value conclusions for the respective approaches; he testified he would not change his final opinion of value for the subject property. We do not find this reasonable. Moreover, PAAB was unable to replicate Anderson’s conclusions after his adjustments. Therefore, we find it difficult to place any reliance on his conclusions without the need for a supplementary report fully describing his adjustments.

We conclude the Board of Review upheld its burden to support the assessment. *Equitable Life Ins. Co.*, 281 N.W.2d at 824 (identifying that section 441.21(3) “does not dictate any particular technique which must be used by the assessor to carry the burden when it has shifted.”). In addition to pointing out problems with Wal-Mart’s experts’ reports, the Board of Review offered Westercamp’s appraisal in support of the assessment. Although not without some flaws, Westercamp’s appraisal is the most persuasive indication of value in the record. Acknowledging the lack of precision in

property valuation, Westercamp's sales comparison approach¹⁷ and reconciled value support the subject's assessment. *Wellmark*, 875 N.W.2d at 672 ("The valuation of property has never been an exact science.") (citations omitted). Unlike Jenkins' appraisal, we find Westercamp's opinion a more credible reflection of the subject property's current use as required by Iowa law.

Order

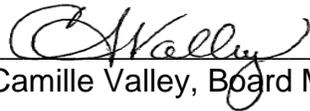
PAAB HEREBY RESCINDS its September 9, 2017 Order that set the property's value at \$15,500,000 as of January 1, 2015 and January 1, 2016.

PAAB HEREBY AFFIRMS the January 1, 2015 and January 1, 2016 assessments as determined by the Johnson County Board of Review.

This is PAAB's final agency action under Chapter 17A, issued on remand from the District Court of Johnson County.



Karen Oberman, Presiding Officer



Camille Valley, Board Member

Copies to:

Paul Burns/Melissa Carrigton/Matthew Barnd for Wal-Mart by eFile

Susan Nehring/Ryan Maas for the Board of Review by eFile

Johnson County Auditor
913 S. Dubuque Street
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¹⁷ In *Kohl's Dept. Stores v. Dallas Cnty. Bd. of Review*, the Iowa Court of Appeals stated that Nelson's sales comparison approach value of \$8,185,000 supported Dallas County's assessment of the property at \$8,357,450. 2016 WL 740372 *4 (Iowa Ct. App. Dec. 21, 2016). Similarly here, while Westercamp's sales comparison approach value is below the current assessment, we believe it supports the assessment.