



Dark Stores: An Interview with Donna VanderVries

Chris Bennett

The statements made or opinions expressed by authors in Fair & Equitable do not necessarily represent a policy position of the International Association of Assessing Officers.

Donna VanderVries was a featured presenter at the Wisconsin Association of Assessing Officers (WAAO) March Quarterly Meeting on March 7, 2016. Ms. VanderVries copresented with Judy Sharpe, Assessor for Monroe County, Indiana, and President of the Indiana Assessors Association and Stacey O'Day, Assessor for Allen County in Indiana and Legislative Chair for the Indiana Assessors Association

The presentation, "Dark Stores: The Michigan and Indiana Experience," was well received by the WAAO audience as they develop strategies to defend against dark store appeals in their state. Ms. VanderVries is the Equalization Director for Muskegon County, Michigan.

Q. *Donna, what is your current role in the valuation resolution and appeals process?*

I am the assessor of record for a number of units in Muskegon County, Michigan. As such, I deal with appeals and am involved in commercial and industrial appeals as they go through the Michigan Tax Tribunal (MTT) process. I also negotiate settlements when that appears

to be the best course of action, or we find inaccuracies in our data or market data supporting a different value.

Q. *After a big box store goes "dark," does the highest and best use change, or is it still a big-box store?*

It depends. The highest and best use as a second-generation facility is not likely to be a big-box store primarily because of owner-imposed deed restrictions. There has been at least one big-box property I am aware of that transferred between two different big-box retailers. That was an older comparable.

Q. *How do seller-imposed deed restrictions (restrictive covenants) affect market value? Do properties with deed restrictions reflect the market or distort it?*

I believe they affect the market as the property could not sell for many different types of retail use based on the specific deed restriction. They reduce value.

Deed restrictions mean a property may sit unused for years. We have a deed-restricted store in one of my assessing units that has been sitting vacant since 2007.

In Cottage Grove, Minnesota, for instance, a Home Depot that's been shuttered for seven years will sell its space to the city only if the city agrees to keep any competition out of the surrounding mall for another 15 years. The ban has left local officials fuming, reports the St. Paul *Pioneer Press*, which described the sale conditions as "crippling city development for the next 15 years."

The highest and best use as a second-generation facility is not likely to be a big box store primarily due to owner-imposed deed restrictions.

Q. *Why are restrictive covenants considered when determining value for property tax purposes?*

Michigan law currently allows for enforcement of restrictive covenants and does not provide an exception for property tax valuation purposes.

(continued on next page)

Q. *Immediate economic obsolescence is often cited in contested valuation of specialized big box stores. How should assessors respond to this argument?*

Look for market evidence of the obsolescence. Can it truly be isolated as in paired sales? What else is involved in the sale price as a second-generation sale? Most of the sales are older and have age differences. They may be in inferior locations. Often these second-generation properties are located in declining markets.

Big box retailers will leave these buildings behind (deed restricted) and rebuild a couple of miles away in the newer, hotter commercial location.

In addition, the highest and best has changed and expenditures are made immediately after purchase because of the change in highest and best use—for example, to convert a property to industrial, a church, multitenant, and so on. How much obsolescence is a brand-new store reasonably expected to have? Is it realistic that a big-box store built in 2014 at a cost of \$12 million for the building and \$5.5 million for the land is really worth only \$4 million? That is what the retailer claims in the appeal. Analogous to a car, a property may instantly lose value when it is built/driven off the lot, but what is reasonable?

Q. *If these stores are really worth so much less, wouldn't a prudent business buy and convert a second-generation store to its needs?*

Also, looking at the market, how can these properties be worth less than land value? We have values in Michigan pushing industrial values per square foot. Isn't commercial land in a prime retail corridor worth more than an industrial piece of property? Do these values really make sense?

To cite the newspaper: The Menards store in Oshtemo Township [Kalamazoo County], for example, was valued at just

under \$8.3 million in 2011. It appealed to the MTT, and the property's true cash value was reduced to \$6.4 million. This decision cost our township \$75,000 in revenue over 5 years that would have been spent on police, fire, and roads.

In 2014, Costco purchased property for \$5.5 million and the construction was valued at over \$12 million, resulting in a total building and land value of \$17.5 million. Attempting to strike a balance between the conventional methods of assessment and those of the MTT, the assessor in Oshtemo valued the property at \$8.6 million, a conservative valuation. Despite this effort, Costco is asking the MTT for a true cash value of \$4 million. It is requesting a value that is less than what was paid for the dirt on which it was built.

Is it realistic that a big-box store built in 2014 at a cost of \$12 million for the building and \$5.5 million for the land is really worth only \$4 million?

Q. *Can you explain what a special-purpose doctrine is, and how it might apply to big-box stores?*

"The special purpose exception is applied to a building in good condition being used currently and for the foreseeable future for the unique purpose for which it was built," a doctrine necessary to prevent "the owner of a distinctive, but yet highly useful, building" from "escap[ing] full property tax liability" (Fed. Res. Bank of Minneapolis v. State [Minn.1981], 313 N.W.2d 619, 623).

Big-box stores are similar to the bank at issue in that case, in which it was held that the cost approach could be used to value the property. It is also noteworthy in that case that the parties stipulated to the land value.

In cases in Michigan and Indiana, there has been a complete disregard for the land value. The total value of the land and building combined, as claimed by the petitioner, may actually be less than dirt.

Other state courts have generally approved reliance on a single approach in similar situations. Usually, as in our case here, comparable sales are not available for a building that is a special-use property. Nor is the income approach always directly relevant.

Quoting from the case: Thus, where "the owner is less interested in the income the property will generate than in occupying a building uniquely suited for the owner's special type of business," the reproduction cost minus depreciation method has been held to be appropriate for determining the market value of a bank, rather than an income approach.

Other decisions have supported this view—*First Federal Savings & Loan Ass'n of Flint v. City of Flint*, 104 Mich.App. 609, 615, 305 N.W.2d 553, 556 (1981). See also *State v. Federal Reserve Bank*, 25 F. Supp. 14, 19 (D.C.Minn.1938); *Shawmut Inn v. Town of Kennebunkport*, 428 A.2d 384 (Me.1981); In Matter of Joseph E. Seagram & Sons, Inc.

Q. *Are local communities over-reliant on property tax revenues from big-box stores? Do other benefits to the community (store-funded infrastructure improvements, job growth, and economic stimulus) offset the perception of lost revenue?*

I don't believe so. If anything, there is an issue about the store paying its fair share of taxes. We are charged with uniform and equitable assessment. To carve out a special niche for these stores destroys uniformity. Technically, the same argument could be applied to any type of property.

IAAO Past President Marty Marshall also commented,

For assessors, this is not a revenue issue. It is a valuation issue. The issue is making headlines because of the revenue implications, but for assessment administrators it is about the value of the property and equitable distribution of the tax burden.

For school districts and other recipients of property tax revenues, decisions that force jurisdictions to refund monies after budgets are already committed create serious revenue stream problems

Q. *Walmart recently announced the closing of 269 of 11,600 stores. It also plans to open 300 new stores globally. How does the frequent closing and opening of big-box stores affect the number of appeals?*

I have not specifically analyzed that but would tend to believe that would give Walmart a greater pool of comparables in these second-generation big-box stores. However, these types of properties and potential sales are exactly what have typically been burdened with deed restrictions that require a value-lowering change in highest and best use.

Q. *Can state legislation create an equitable solution to the big-box issue to ensure stable revenues from the property*

tax? What are some legislative alternatives being considered?

Michigan is considering various changes including changes related to deed restrictions. Often, these vacant stores sit for years and are arguably blighted. The legislature is looking at limited-use property and presumptions requiring the use of the cost approach for newer property and also the possibility of qualified real property paying fees for services. There is a subcommittee working on proposed solutions to this issue.

Q. *Are "dark stores" the best example of unencumbered fee simple value?*

No. A property does not need to be vacant to be considered unencumbered and available in fee simple. Big-box stores are the only types of properties that are currently being evaluated in this manner

Clearly when we value residential properties, we don't require the comparable sale to have been vacant or dark at the time of sale to be considered unencumbered and available in fee simple. Why should big-box retail be valued differently than every other class of commercial, residential, or industrial improved property? This theory artificially devalues properties, and the additional concern is that once applied to

these big-box retail properties, there is no logical end to prohibit its application to other property types. ■

Managing Editor's Note:

The Michigan legislature is currently considering House Bill 5578 (<http://www.legislature.mi.gov/documents/2015-2016/billintroduced/House/htm/2016-HIB-5578.htm>, accessed May 3, 2016), which proposes to close the dark store valuation loophole and require the Michigan Tax Tribunal to consider all three approaches to value when determining the cash value of big-box properties and all other property types.

The bill proposes reforms to property tax law covering three basic actions:

- All property must be assessed at its highest and best use.
- Private deed restrictions should not be a factor in determining a property's true cash value.
- The Michigan Tax Tribunal should be required to consider comparable sales, capitalization of income, and cost less depreciation when determining a property's true cash value for assessment purposes.

FOUNDATION NEWS

The Appraisal Practices Board (APB) of The Appraisal Foundation has issued a first exposure draft: Valuation of Green and High-Performance Property: Commercial, Multifamily, and Institutional Properties

All interested parties are encouraged to comment in writing to the APB before June 20, 2016 by mail, e-mail, or facsimile.

All comments will be read and considered.

Mail to: Staci Steward, The Appraisal Foundation, 1155 15th Street NW, Suite 1111, Washington, DC 20005

E-mail: APBcomments@appraisalfoundation.org

Fax: 202.347.7727

If you have any questions regarding this exposure draft, please contact Staci Steward at (202) 624-3052 or staci@appraisalfoundation.org.