

Debating the **Hot** Topics

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PROPERTY TAXATION AND THE LAW:
CHALLENGES AND SOLUTIONS



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Retail/Big Box/Dark Store Theory/Fee Simple



Dark Store Theory- What is it?

A combination of various appraisal theory issues including:

- Appropriate Appraisal Approaches
- Selection of Sales Comparables
- Selection of Rent Comparables
- Highest and Best Use
- Fee simple – (Unencumbered?)

Appropriate Appraisal Approaches

- Sales Comparison Approach
- Income Capitalization Approach
- Cost Approach

Selection of Sales Comparables

- Vacant Properties
- Occupied Properties
- Specific Sub-Category of Retail
- Generic Retail Stores
- KEY ISSUES – LOCATION, SIZE, AGE

Selection of Rent Comparables

- Vacant Properties
- Occupied Properties
- Specific Sub-Category of Retail
- Generic Retail Stores
- KEY ISSUES – LOCATION, SIZE, AGE

Highest and Best Use

- Vacant Properties
- Occupied Properties
 - Specific Sub-Category of Retail
 - Generic Retail Stores
 - KEY ISSUES – LOCATION, SIZE, AGE

Fee Simple

Does it mean “unencumbered”?

If so, what does “unencumbered” mean?

Bundle of Rights

- Wisconsin's Supreme Court has held that the lease is not part of the bundle of rights that is to be assessed for purposes of the property tax. *Walgreen Co. v. City of Madison*, 2008
- Specifically, the Manual states: “Comparable sales refer to properties that are similar to the subject property in age, condition, use, type of construction, location, design, physical features and economic characteristics.” 1 Wisconsin Property Assessment Manual 7-24. “The more similar the sold property is to the subject, the more reliable is the sale price as an indicator of the value of the subject property.”

Lowe’s v City of Delavan

Before continuing in our analysis, we take a brief detour to discuss the terminology that we employ. Some confusion has arisen due to inconsistent usage of the terms “vacant” and “dark.” Although the court of appeals in this case seemingly used the terms interchangeably, they have different meanings.

- ¶46 We acknowledge that the Manual may not be a model of clarity on the subject, but its language does indicate that “vacant” and “dark” are not synonymous. The Manual states that “[a] vacant store is considered dark when it is vacant beyond the normal time period for that commercial real estate marketplace and can vary from one municipality to another.” Id. Thus, “dark,” as used by the Manual, is a subset of “vacant.” In other words, all dark stores are vacant, but not all vacant stores are dark.
- *Lowe’s v City of Delavan*

- Lowe's v City of Delavan - - - Footnote 10:

The Manual discourages the use of “dark” and “distressed” properties “as comparable sales unless the subject property is similarly dark or distressed.” Wisconsin Property Assessment Manual 9-12 (2016). Pursuant to the Manual, “[a] vacant store is considered dark when it is vacant beyond the normal time period for that commercial real estate marketplace and can vary from one municipality to another.” *Id.* As such, “vacant” and “dark” are not synonyms. For further discussion on the distinction between “vacant” and “dark,” see *infra*, ¶¶45-46. The Manual does not specifically define “distressed,” but it counsels that “[a] recent court case stated distressed properties are not seen as meaningfully comparable to operating properties.”

Wisconsin Property Assessment Manual 9-12 (citing *Bonstores Realty One, LLC v. City of Wauwatosa*, 2013 WI App 131, ¶¶21, 22, 34, 35, 351 Wis. 2d 439, 839 N.W.2d 893). All references to the Wisconsin Property Assessment Manual are to the 2016 version unless otherwise indicated.

“[T]he assessor must not consider only the physical attributes of the land and improvements but the intangible benefits that are associated with them.”).

Lowe’s v City of Delavan

- * If a sale is out of a receivership as part of the distribution of a portfolio of family-owned assets, is that a distressed sale ?
- * If the entirety of the assessment record is a one page cost approach, and the assessor cannot explain the abbreviation “Ext. Obs.”, does that assessment qualify for a presumption of correctness ?
- * If the trial appraisal in support of the assessment is based on “less than ideal” comparables in the sales comparison approach where no leases or income and expenses were verified , and where all of the comparables were of similar size to the subject property, **BUT** the subject is a single user retail store and the comparables all had five to ten tenants, are they truly comparable sales and does such a “less than ideal analysis” appraisal deserve persuasive credibility ?

Retail Case Authorities

- *Lowe's Home Centers, LLC v. City of Wauwatosa*
- *Lowe's Home Centers, LLC v. City of Delavan*
- *Wisconsin Property Assessment Manual*
- *Rancho Cincinnati Rivers, LLC v. Warren Cnty*
- *Menard, Inc. v. City of Escanaba*
- *Walgreens Eastern Co. v. Town of Hartford*
- *Macy's Retail Holdings, LLC . Cnty of Hennepin*

■ EPILOGUE

Macy's Retail Holdings v County of Hennepin (July 10, 2025)

“The outcome of this case turns on whether the HBU of the subject property, as improved, is for redevelopment (as advanced by Macy's) or for continued use as an anchor department store (as advanced by the County). Both outcomes are indisputably legally permissible and physically possible. The parties, however, present differing financially feasible and thus maximally productive conclusions.”

Macy's Retail Holdings

- “Mr. Waytas considered **market demand** at Southdale Center in particular. In 2017,
- the mall ownership purchased the JC Penney property, a large (255,675 square feet
 - of total area) owner-occupied anchor space, following its closure in 2017, and
 - immediately razed it for redevelopment. In 2018, when the Herberger's space,
 - another large department store anchor with a total area of 131,548 square feet,
 - became vacant, the mall multi-tenanted the space.

Macy's Retail Holdings

After determining the market value of the land, an appraiser must then determine the cost to replace or reproduce the improvements. *TARE* at 532. Here, Ms. Stoerzinger chose to calculate the replacement cost for a smaller department store, as a 145,000 square-foot store is more typical for the current market, rather than calculating the replacement cost for the store's actual 275,151 square feet.

- ***
- Lastly, to calculate external obsolescence—loss in value due to negative externalities,
- here, a downturn for department stores—Ms. Stoerzinger looked to the difference
- between national and local department store vacancies, which was 19.6 and
- 10.7% for each assessment year, respectively.

- Macy's Retail Holdings
- Thus, with replacement cost new values of \$26,548,498 and
- \$30,757,363, Ms. Stoerzinger subtracted out the physical deterioration
- and external obsolescence (with the functional obsolescence having
- been already recognized by constructing a smaller building (i.e., 145,000
- sf store)).

Macy's Retail Holdings

BOTTOM LINE – SO FAR

ORDER FOR JUDGMENT

The assessed value of the subject property as of January 2, 2021, shall be increased from \$10,094,700 to \$12,716,000.

The assessed value of the subject property as of January 2, 2022, shall be increased from \$10,097,900 to \$16,022,000.

Real estate taxes due and payable in 2022 and 2023 shall be recomputed accordingly.

Big Box Retail – Minnesota

- Macy's Retail Holdings
- **POST EPILOGUE:**
- Macy's Motion for Amended Findings Denied by Order of Minnesota Tax
- Court dated December 4, 2025.
- Will an appeal to the Minnesota Supreme Court be filed ?

Hotels



Intangibles

- Branding
- Franchise
- Management agreement
- Workforce in place
- Creditworthiness
- Restaurant/Convention Space

Intangibles

- **The Appraisal of Real Estate cites 4 options for appraising only the real estate where intangibles exist:**
 - Parsing Income Method (Assign income to intangible assets first)
 - Management Fee Approach (Deduct management and franchise fee - Rushmore)
 - Market Participant Survey Approach (Interviews w/ market)
 - The Cost Approach

Appraisal Methodology

- *JPMC 2018- MINN SS TRA, LLC v. Cnty of Hennepin*
- *1300 Nicollet, LLC v. Cnty of Hennipin*
- *JDHQ Hotels LLC v. Sarpy Cnty Bd. Of Equalization*
- *Walt Disney Parks and Resorts US, Inc. v. Mercado*
- *Olympic and Georgia Partners, LLC v. Cnty of L.A.*
- *SHR St. Francis LLC v. City and Cnty. of San Francisco*

RECENT SUMMARY OF KEY ISSUES:

JPMC 2018- MINN SS TRA, LLC v. Cnty of Hennepin

We find that the Parsing Income Method used by JPMC better Isolates taxable Real Estate value than does the Management Fee Approach used by the County. We therefore use the Parsing Income Method to determine the subject property's market value as of the four assessment dates and conclude that the County's assessed value overstates the market value as of each date.

JPMC 2018

■ ORDER FOR JUDGMENT

- 1. The assessed value of the subject property as of January 2, 2017, shall be decreased from \$153,500,000 to \$83,123,000.
- 2. The assessed value of the subject property as of January 2, 2018, shall be decreased from \$115,600,000 to \$89,047,000.
- 3. The assessed value of the subject property as of January 2, 2019, shall be decreased from \$115,600,000 to \$98,460,000.
- 4. The assessed value of the subject property as of January 2, 2020, shall be decreased from \$119,070,000 to \$105,116,000.

- JPMC 2018
- * In this case, the Management Fee Approach fails to effectively separate the value of taxable real estate from non-taxable intangible assets.
- * A second problem with the Management Fee Approach is that allowing an expense deduction for management fees “does not allow for a *return on* the capital expenditure.” *TARE*, at 677 (emphasis added). A management contract is an intangible asset,⁵⁹ *id.* at 670, and intangible assets are a form of personal property, *id.* at 664-65 (listing “[f]ranchises and other contracts” as intangible personal property). “[An] allocation to personal property must account for both *return on* and *return of* investment for that asset class.” *Id.* at 672 (emphasis added)

JPMC 2018

We acknowledge (as did Mr. Lennhoff) that many appraisers use the Management Fee

- Approach to value hotels, and that they frequently assert that their work values hotel real estate
- only. In our view, however, this proves only that such appraisers **subscribe to the theory** that the
- deduction of management fees removes from a hotel operation all intangible business value; it
- **does not prove that the deduction *actually does so***. Based on the foregoing analysis, we find that it
- does not.
- ***
- Our application will involve: (1) use of the proxy rent technique to remove the
- intangible business value of the F&B Department, *id.* at *16-18; and (2) additional deductions to
- remove income attributable to intangible assets such as (a) business startup costs and (b) brand
- affiliation, *id at* *24-26.

Appraisal Methodology

Aurora Convention Ctr. Hotel LLC v. Adams Cnty Bd. Equalization

On *Disney* trial and appellate decisions: “Neither court held broadly that the Rushmore approach could not be used to value hotel property – only that the evidence in that case (which is not detailed in the opinion) convinced them that the Rushmore approach didn’t adequately remove the value of business operations... .”

Appraisal Methodology

Aurora Convention Ctr. Hotel LLC v. Adams Cnty Bd. Equalization

On *SHC Half Moon Bay* decision: “Significantly, the state assessor’s handbook... rejects the Rushmore approach as a method of valuing hotel properties... and the assessor’s expert had conceded that the assessor’s approach ‘did not remove all intangible assets and rights.’ ”

Branding/Flag/Franchise

Is deducting the franchise fee sufficient???

Management Agreement

Is deducting the management fee sufficient???

JPMC 2018

Finally, when allocating income to asset classes, it is irrelevant that neither an existing hotel owner nor a prospective purchaser owns (or will own) either the management company or the brand that contributes to existing hotel revenue.

- ***
- Since both appraisers began with income *to the total assets of the business*, both
- had to remove income attributable to Hilton's management expertise and brand
- *regardless of who actually owned the management company or brand*. Otherwise,
- the method used would not isolate income to the real estate only.

JPMC 2018

The Management Fee Approach would attribute to hotel real estate *the entire net income of the hotel owner's F&B business* (as calculated without a rent amount) (line 14). It would thus *misattribute* to hotel real estate \$4,915,698 of income ($6,505,218 - 1,589,520 = 4,915,698$).⁸² *** To compound this problem, the resulting overvaluation of real estate would *not* be limited to the amount of net income misattributed (approximately \$5 million). Instead, the error would be amplified through capitalization. Mr. Kieser's weighted capitalization rate for 2018 was 10.60%. Using this rate to capitalize the \$4,915,698 misattributed to the hotel real estate would produce a overvaluation of \$46,374,509 ($4,915,698 \div 0.106 = 46,374,509.40$).

Workforce In Place

■ *Boise Cascade Corp. v. Dept. of Revenue*

“How would an appraiser evaluate or determine the importance of management or work force in place? Would it require a thorough evaluation of all personnel in the plant? This would entail reviewing the training, experience, health and accident records and grievances of all personnel. The appraiser would have to interview every employee... To be useful the results would need to be compared with other investigations of similar plants.”

■ JPMC 2018

We adopt Mr. Lennhoff's business startup cost adjustment because a hotel beginning operations from scratch would incur extensive costs for such items as assembling and training its workforce, and thus would not achieve the income of a mature enterprise for some years. *See Rushmore 2012*, at 342. The income of a mature going concern therefore includes income to the intangible asset of startup costs that must be removed to value real estate only.

- JPMC 2018
- Several courts have recognized the need for such an adjustment in an income approach valuing real estate only. *See, e.g., Singh v. Walt Disney Parks & Resorts US, Inc.*, 325 So. 3d 124, 130 (Fla. Dist. Ct. App. 2020) (identifying “assembled workforce” as an intangible asset not adequately removed by the appraiser’s use of the Management Fee Approach); *Sunstone Hotel P’ship v. Cnty. of Los Angeles*, No. BC635223, at (Cal. App. Dep’t Super. Ct. Feb. 21, 2018) (quoting with approval Mr. Lennhoff’s explanation that “[a]nytime that you’re beginning with a revenue from a stabilized operation, you have to recognize all of the expenses that are costs that would have been incurred to get to that stabilized level and that would include a startup cost”); *SHC Half Moon Bay, v. Cnty. of San Mateo*, 226 Cal. App. 4th 471, 490 (Cal. Ct. App. 2014) (holding that “the deduction of the management and franchise fees from the hotel’s projected revenue stream pursuant to the income approach did not ... identify and exclude intangible assets such as the hotel’s assembled workforce”).

Creditworthiness

- *RC Springfield 2007 LLC v. Lane Cnty. Assessor*
 - “The court is not persuaded that the creditworthiness of the Sale 3 tenant is significant to this analysis. Given the size of the subject property, and the fact that it would compete in a regional or national market, the court assumes that any potential owner or lessee would possess adequate credit to purchase or lease the subject property.” (160,007 sq. ft. Office call center)
- *McGrath’s Pub. Fish House v. Marion Cnty Assessor*
 - “There is a correlation between national credit tenants and higher rents – that is plain to see in the data presented by the parties. But the data also shows a correlation between higher lease rates and superior locations. The court does not accept the premise that national credit tenants, and their superior credit, will in every case be the cause of higher rents at a specific property; the correlation could just as easily have other explanations...”

Restaurant/Convention Space

- *Singh v. Walt Disney Parks and Resorts, U.S.*
 - Court advocates use of proxy rent, but rejects non-hotel restaurant rents as comparables.
- Select comparables (but what is comparable??)
- Determine base and % rent typical in industry and apply to restaurant income. (Factoring in Convention Space meals/Room Service)
 - **Convention and restaurant space via cost approach?**

- Olympic and Georgia Partners, LLV v County of Los Angeles (August 28, 2025).

The key inquiry in this case, then, is not merely whether the occupancy tax and key money payments derive from intangible assets, but rather whether those forms of revenue represent income that is primarily attributable to enterprise activity or whether they constitute “income of the real property or on account of its beneficial use.” (Olympic & Georgia Partners, LLC v. County of Los Angeles (2023) 90 Cal.App.5th 100, 119 (dis. opn. of Grimes, J.) (Olympic).) Applying those principles here, we conclude that the Assessor was permitted to include the occupancy tax and key money payments when assessing the value of the hotel. Unlike the situation we addressed in *Elk Hills*, both payments derive from a type of intangible asset that effectively enable the property itself—as opposed to the business operating the property—to generate more revenue. Under the occupancy tax agreement, the hotel generates an additional 14 percent in revenue every time a customer rents out a room. This revenue source will continue regardless of who owns the hotel or how they run their business. With respect to the key money payment, the Assessor presented undisputed evidence that management companies routinely pay owners of hotels that have certain desirable physical features (such as location, size or overall quality) key money as a means of securing the right to manage the property and advertise the hotel under the management company’s brand. Thus, much like a commercial lease, key money is a form of revenue that owners of desirable hotels expect to receive in exchange for assigning a management company the right to make beneficial use of the property. Because both the occupancy tax and key money payments “represent[] income from the use of the taxable property itself)”].

- Olympic and Georgia Partners, LLV v County of Los Angeles (August 28, 2025)
- The County raises a separate claim regarding the valuation of various “enterprise assets” that derive from its management agreement with Marriott, including the customer goodwill associated with the Marriott brand, the value of the hotel’s food and beverage operations and an assembled, stable workforce. Unlike the two revenue streams described above, the County does not dispute that these three enterprise assets are nontaxable and that their value must therefore be excluded from the assessment. The County argues, however, that the Assessor properly accounted for the value of those assets by deducting the management fees that Olympic pays to Marriott. Olympic disagrees, contending that the County produced insufficient evidence to support its claim that the management fees captured the entire value of the three enterprise assets. The trial court and Court of Appeal agreed with Olympic and remanded the matter to the County’s assessment appeals board (Board) for further proceedings regarding the valuation of these three assets. We affirm the lower courts’ findings on this issue.

- SHR St. Francis, LLC, v City and County of San Francisco (Cal Court of Appeals, August 1, 2023)
- We find that the method used by the City to exclude the value of nontaxable, intangible assets from the assessed value of the hotel—i.e., the deduction of fees or expenses associated with the asset from the hotel’s future income stream—is legally incorrect. As a result, the assessed value of the hotel improperly subsumed the value of the management agreement, in-room movies, and guest laundry services. We, however, find that the assessed value properly included the cancellation/no show/attrition income because that asset is a taxable attribute of the property. We therefore affirm in part and reverse in part and remand for a redetermination of the taxable value of the hotel.

Office Assessments (...in the post-COIVD world)



Office Assessments (...in the post-COIVD world)

- Declining Vacancy – Contractual vs. Actual
- Winners and Losers
 - (Across the board or select properties?)
- Corporate Headquarters

- Features
 - Long term
 - Locked-in terms
 - Based on cost?
- Reflective of market value?

Litigation Strategies



- Madison County Assessor v Kohl's Indiana, LP (Indiana Tax Court, November 17, 2025).

Appraisals, like books, cannot be judged by their covers. For an appraisal to meet the burden of proof, its analysis and conclusions of value must stand on their own. They must convince the finder of fact to the level of a preponderance. **Assertions that an appraisal is prepared by an expert appraiser in accordance with generally accepted appraisal principles may yield some credibility and demand some weight, but such conclusory statements are not enough.** The Board must actually take account of its own evaluation of the data, analysis, and reasoning employed in the appraisal to determine if the burden of proof has been met. Were it otherwise, the Board's two-prong test would turn the evaluation of an expert appraisal into a formulaic, check-the-box exercise that automatically accorded persuasive weight to such appraisals, regardless of the soundness of the analysis, the quality of the data, or the accuracy of the conclusions. This framework would improperly allow a mere scintilla of evidence to carry the day. Because the Board applied the wrong legal standard, the Court finds that the Board abused its discretion. An abuse of discretion occurs when the Board issues a finding that is "against the logic and effect of the facts and circumstances before it or in contravention of the law." *DuSablón v. Kaufman*, 160 N.E.3d 587, 591 (Ind. Tax Ct. November 17, 2025)

- Discovery
- Depositions
- Pre-trial motions
- Trial Tactics
- Post-trial/Appeal issues

Thanks for joining us!!!

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