BOARD OF ASSESSMENT APPEALS, STATE OF COLORADO 1313 Sherman Street, Room 315 Denver, Colorado 80203 Petitioner: **WHW 2 PARTNERSHIP C/O WALGREEN CO.,** v. Respondent: **JEFFERSON COUNTY BOARD OF EQUALIZATION.**	**Docket No.: 75147, 72412**

ORDER

THIS MATTER was heard by the Board of Assessment Appeals on April 30, 2019, Sondra W. Mercier and Samuel M. Forsyth presiding. Petitioner was represented by Kendra L. Goldstein, Esq. Respondent was represented by Rebecca P. Klymkowsky, Esq. Petitioner is protesting the 2017 and 2018 actual value of the subject property.

PRELIMINARY MATTERS

The Board consolidated Dockets 72412 and 75147. Paul G. Bakken and Matthew Schroeder were accepted as Petitioner's expert witnesses. Katherine E. Fontana was accepted as Respondent's expert witness. Petitioner's Exhibits 1 and 2 as well as Respondent's Exhibits A and B were admitted.

During the hearing, the Board heard the parties' arguments pertaining to Petitioner's Motion to Compel production of Documents, or in the Alternative, Strike Portions of Respondent's Appraisal Report ("Motion to Compel"). Petitioner filed its Motion to Compel on April 10, 2019 and a Supplement to Petitioner's Motion to Compel on April 17, 2019. Respondent filed a Response to Petitioner's Motion to Compel on April 18, 2019 and Petitioner filed a Reply to Respondent's Response to Petitioner's Motion to Compel on April 19, 2019. The Board issued an Order denying Petitioner's Motion to Compel on April 23, 2019. On April 24, 2019 Petitioner filed its Revised Motion for Reconsideration of the Board's April 23, 2019 Order.

Having considered the parties' arguments, the pleadings and the record, the Board finds that the confidential information pertaining to Walgreens stores in Jefferson County, each identified within Respondent's income approach by their respective addresses, was not provided in a manner that the source could not be identified as required by Section 39-8-108(5)(c), C.R.S. In addition, upon further examination of Respondent's appraisal report, the Board finds that with the exception of Respondent's lease comparable 1, Respondent failed to provide certain pertinent information subject to disclosure pursuant to Section 39-8-108(5)(c), C.R.S. Therefore, in arriving to a determination concerning the subject's valuation in this matter, the information contained on pages 42-49 of Respondent's appraisal report was excluded from the Board's consideration.

DESCRIPTION OF THE SUBJECT

Subject property is described as follows:

7496 South Simms Street, Littleton, Colorado
Jefferson County Schedule #300416328

Petitioner states the improvement size is 13,450 square feet. Respondent states the improvement size is 13,368 square feet. Given the caveats explained by Petitioner's expert witness on how he determined the size from architectural plans, the Board accepts Respondent's statement of size. The subject is a freestanding, single-tenant Walgreens retail/pharmacy store. The one-story building was completed in 1996. There is a canopy covered drive-through and secure pharmacy area. The improvements are located on a 68,195 square foot site which yields a .196 floor area ratio.

EVIDENCE RPESENTED

Petitioner presented the following indicators of value:

Market:	$1,950,000
Cost:	$1,800,000
Income:	$2,000,000

Petitioner is requesting an actual value of $1,975,000 for the subject property for tax years 2017 and 2018. Respondent provided an appraisal concluding to a value of $2,828,000 which supports the assigned value of $2,732,900 for the subject property for tax years 2017 and 2018.

Petitioner called its first witness, Paul G. Bakken, CRE, MAI, CCIM, MS, and Certified General Appraiser who presented an Appraisal Report/Complete Analysis. Mr. Bakken testified that the subject is custom designed and constructed for the purposes of a particular occupant. He believes that the custom nature of the subject is not suitable for other users absent significant modifications. He testified that properties constructed for Walgreens' use have higher value to Walgreens itself than the value-in-exchange or market value. Petitioner's expert testified that other functional obsolescence factors leading to a loss in value that are unique to Walgreens (such as store size, limited entrances, interior/exterior branding, single-user design (width and depth), loading docks, drive through placement, window placement and concentrated parking) should be taken into account. Petitioner concluded that the highest and best use of the property is "as is" on the date of value as a single-user free-standing retail use.

Petitioner developed value indications based on the three approaches to value: Cost Approach, Sales Comparison Approach and Income Approach. For the Sales Comparison Approach, Petitioner presented 10 comparable sales ranging in sale price from $1,240,000 to $6,100,000; in size from 10,380 square feet to 28,068 square feet; in year of construction from 1964 to 2014; and in sale price per square foot from $93.14 to $232.75. Before adjustments, the average sale price per square foot of the 10 comparables was $156.48. After adjustment for time, visibility and access, age, condition and quality, building size, land to building ratio, economics, and other/ misc., the average sale price per square foot was $150.54 and median sale price per square foot was $146.55. Petitioner concluded to a value of $1,950,000, rounded, via the Sales Comparison Approach.

Petitioner presented an Income Approach utilizing the income capitalization method. Petitioner presented a rent study of 20 competitive properties to arrive at a market rent for the subject. Ten of the rental comparables were reported to be actual leased properties during the extended base period; the remaining 10 were comparables listed for rent during the extended base period. Of the actual rent comparables, 3 were free standing properties and the remaining 7 were rental comparables that were part of larger retail developments. The rent range of the rental comparables with actual rents reported was from $5.46 to $15.00 per square foot; the age range of the rental comparables was from 2 to 43 years; and available space ranged from 7,200 square feet to 28,068 square feet. The unadjusted average rent was $11.82 per square foot. Petitioner selected 9 of the rental comparables for adjustments. The selected rental comparables were adjusted for time, location, visibility and access, age, condition and quality, space leased, freestanding/end cap vs. in line mall, effective traffic counts and "involved lots of construction." After adjustments, the rent average was $12.58 and the median was $12.20. Petitioner concluded to NNN rent of $12.50 per square foot. Relying on CBRE data from the Southeast retail sector of the Denver Metro area, Petitioner applied a 6% vacancy rate. Petitioner concluded to a capitalization rate of 7.50% derived primarily from a market survey. Petitioner added an effective tax rate of 2.91% to the capitalization rate. Petitioner concluded to a value based on the Income Approach of $2,000,000, rounded.

Petitioner presented a Cost Approach using 10 local vacant land sales and the Marshall Valuation Service to derive a market-adjusted cost value for the subject property of $1,780,000. Petitioner's land sales ranged in size from 33,197 square feet to 115,434 square feet. The sale prices ranged from $395,000 to $1,450,000. The sale prices per square foot ranged from $11.90 to $24.60. The unadjusted average value was $15.92 per square foot. After adjustments, Petitioner reconciled to $14.00 per square foot or $950,000, rounded. A state -approved cost estimating system was used to value the improvements. After depreciation of 70% accounting for physical, functional, and economic obsolescence, the value determined by the Cost Approach was $1,800,000, rounded.

Petitioner then called Matthew Schroeder, MAI, Certified General Appraiser, as a rebuttal witness. The expert presented and testified to an *Appraisal Review of Jefferson County's Fee-Simple Valuation,* presented as Petitioner's Exhibit B. Mr. Schroeder identified 2 of the vacant land sales within Respondent's cost approach to be outside of the statutorily-prescribed data collection period. The witness contended that a number of Respondent's rent comparables represent lease renewals which are not reflective of the market due to undue stimulus. Many others of Respondent's rental comparables represent build-to-suit leases from 1998-1999 which are irrelevant. Petitioner stated that 5 market approach sales were leased-fee sales that Respondent did not properly account for with any property rights adjustments.

Respondent presented the following indicators of value:

Market:	$2,927,592
Cost:	$2,739,747
Income:	$2,822,542

Respondent's expert, Katherine E. Fontana, Certified General Appraiser with the Jefferson County Assessor's Office, presented a USPAP-conforming Appraisal Report. Respondent developed values based on the three approaches to value: Cost Approach, Sales Comparison Approach and Income Approach.

Respondent presented 5 comparable sales for the Sales Comparison Approach. Respondent's expert stated the most appropriate comparable sales are sales that are retail use at time of sale and remain retail use subsequent to sale. The 5 sales ranged in sale price from $2,000,000 to $4,250,000; in size of improvements from 9,080 to 16,991 square feet; and in sale price per square foot from $198.41 to $262.28. Subsequent to qualitative adjustments for units of comparison such as location, building size, age/condition, access, exposure and land site, Respondent concluded to a value based on the Sales Comparison Approach of $219.00 per square foot or $2,927,592.

Respondent used a state-approved cost estimating service to derive a market-adjusted cost value for the subject property of $2,739,747. Respondent identified 6 vacant land sales. Two of the sales had sale dates prior to the 5-year extended data collection period. Those sales were eliminated from the Board's consideration. Regarding the 4 eligible sales, the size ranged from 49,749 to 130,680 square feet; the unadjusted sale price per square foot ranged from $17.91 to $57.29. Comparable 4's sale date was beyond the appraisal date with a recording date of 11/14/2016. However, that sale was under contract in 2014. The concluded value of the land was $20.22 per square foot or $1,378,903. Respondent utilized the Marshall Valuation Service cost system to conclude to a Replacement Cost New Less Depreciation of the improvements, depreciated at 32% reflecting physical obsolescence, of $1,339,265. The land value of $1,378,903 in addition to the depreciated cost of the improvements of $1,339,265 plus site improvement cost of $21,579 resulted in a total value based on the Cost Approach of $2,739,747.

Within Respondent's Income Approach, Respondent concluded to a capitalization rate of 7.13% derived primarily from published survey data studies. The concluded overall rate was not loaded with an effective tax rate. A secondary source was data obtained from The Net Lease Drug Store Report 3rd Quarter 2016 published by the Boulder Group. After applying a 3% vacancy/collection loss and a 3% expense rate, Respondent concluded to a value based on the Income Approach of $2,822,542.

Respondent assigned an actual value of $2,732,900 to the subject property for tax years 2017 and 2018.

Subsequent to direct examination, Respondent's expert testified to Exhibit B, a rebuttal analysis. Respondent's expert disputed Petitioner's contention that the subject Walgreens store is custom built to the degree that substantial refitting would be required when purchased by a user other than Walgreens. Respondent observed that only three of the sales identified by Petitioner in the Sales Comparison Approach were located in Jefferson County. Of those three sales, sale 5 was a partial interest sale. Petitioner's sale 4 was a bowling alley sale at time of sale; had a use other than retail use subsequent to sale; was not located on a busy arterial; and was not clearly visible to traffic. Sale 8 underwent a change of use subsequent to sale from retail to a house of worship. Respondent's expert identified several examples of what she believed to be inconsistent adjustments and characterizations of comparables within Petitioner's analysis. Regarding the income approach, Respondent again observed that of the 20 total comparable rents, only 6 were in Jefferson County. Respondent also disputed the addition of an effective tax rate to the capitalization rate as the typical lease in the current market indicates that property taxes are a pass-through expense borne by the tenant. Respondent reported numerous concerns pertaining to the cost approach.

THE BOARD'S FINDINGS

Petitioner presented sufficient probative evidence and testimony to prove that the tax years 2017 and 2018 valuation of the subject property was incorrect.

Respondent and Petitioner both developed values using the cost approach. The Board is not convinced that this approach provides sufficient evidence as to the market value of the subject. The subject improvements are 22 years old. Petitioner estimates that the improvements are 70% depreciated based on physical, functional and economic obsolescence. Testimony and evidence provide insufficient market data to suggest these items of obsolescence are present in the market to the extent Petitioner suggests. Respondent provided 2 comparables that were beyond the extended data collection period.

The Board is convinced that the Sales Comparison Approach, as applied by both parties, is flawed and provides little reliable evidence of value. Respondent's sales 1 – 3 were occupied by tenants with longer than typical remaining life of leases and at lease rates greater than market rates in existence at the time of sale. The Board agrees that an adjustment to reflect the fee simple interest rather than the existing leased fee interest should be applied or these sales should be eliminated. The Board further concludes that the comparable selection is too narrow given the leased fee nature of Respondent's comparables 1 – 3 and the dissimilarity of sales 4 and 5. On the other hand, the sale selection identified by Petitioner is too broad. The range of values of price per square foot before adjustments and after adjustments are too great to provide reliable conclusions. The improvements vary in the years of construction between 1964 and 2014, which is a 50-year difference in age. The unadjusted value of sale price per square foot range was $93.14 to $232.75; the adjusted value of the sale price per square foot range was $125.10 to $191.20. From this data set, Petitioner averaged the resulting sale prices per square foot of the comparables to arrive at $145.00 per square foot. Given the range of age, size and sale price per square foot, averaging the resulting adjusted sale prices of all of the comparables yielded a value conclusion that is neither reasonable nor reliable.

The Board concludes that given the size of the subject and its location on a busier than typical thoroughfare, the Income Approach is the best method to determine market value. Petitioner identified 20 rental comparables in the Income Approach. Ten of these rental comparables were actual lease comparables. Of those 10 comparables, 3 were free standing comparables not attached to nor part of larger retail complexes. Those comparables were rental comparables 1, 2 and 4. Petitioner's adjusted rents per square foot of these three comparables were $12.75, $15.04, and $11.53, respectively. Taking into account the size, age and location of the rental comparables, the

Board concludes to NNN rent of $14.50 per square foot. Petitioner has determined a capitalization rate of 7.50% to which Petitioner added an effective tax rate of 2.91% to account for property taxes. Evidence and testimony indicate that the terms of the typical lease in this market is NNN where the tenant is responsible for the payment of property taxes. The Board concludes therefore that the net operating income should be capitalized at a rate that does not include an effective tax rate. Based on these conclusions, the Board finds the following:

	Square Ftg.	Rate	
Potential Gross Income	13,368	$14.50	$193,836
Vacancy Rate		6.00%	
Vacancy Expense			$11,630
Effective Gross Income			$182,206
Expense Rate		6.00%	
Expense			$10,932
Net Operating Income			$171,273
Capitalization Rate		7.50%	
		Value	**$2,283,600 (rounded)**

ORDER:

The Board concludes that the 2017 and 2018 actual value of the subject property should be reduced to $2,283,600.

APPEAL:

If the decision of the Board is against Petitioner, Petitioner may petition the Court of Appeals for judicial review according to the Colorado appellate rules and the provisions of Section 24-4-106(11), C.R.S. (commenced by the filing of a notice of appeal with the Court of Appeals within forty-nine days after the date of the service of the final order entered).

If the decision of the Board is against Respondent, Respondent, upon the recommendation of the Board that it either is a matter of statewide concern or has resulted in a significant decrease in the total valuation of the respondent county, may petition the Court of Appeals for judicial review according to the Colorado appellate rules and the provisions of Section 24-4-106(11), C.R.S. (commenced by the filing of a notice of appeal with the Court of Appeals within forty-nine days after the date of the service of the final order entered).

In addition, if the decision of the Board is against Respondent, Respondent may petition the Court of Appeals for judicial review of alleged procedural errors or errors of law within thirty days of such decision when Respondent alleges procedural errors or errors of law by the Board.

If the Board does not recommend its decision to be a matter of statewide concern or to have resulted in a significant decrease in the total valuation of the respondent county, Respondent may petition the Court of Appeals for judicial review of such questions within thirty days of such decision.

Section 39-8-108(2), C.R.S.

DATED and MAILED this 13th day of August, 2019.

BOARD OF ASSESSMENT APPEALS:

Drafting Board Member:

Samuel M. Forsyth

Concurring Board Member:

Sondra W. Mercier,
concurring without modification pursuant to Section 39-2-127(2), C.R.S.

I hereby certify that this is a true and correct copy of the decision of the Board of Assessment Appeals.

Milla Lishchuk

STATE OF COLORADO SEAL BOARD OF ASSESSMENT APPEALS