

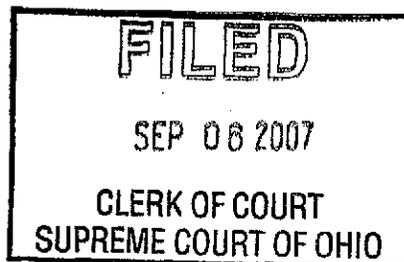
IN THE SUPREME COURT OF OHIO

Cincinnati School District)
Board of Education,)
)
Appellee,)
)
vs.)
)
Hamilton County Board of Revision,)
Hamilton County Auditor, and the Tax)
Commissioner of the State of Ohio,)
)
Appellees,)
)
and)
)
Anchor Lyons Limited Partnership,)
)
Appellant.)

Case No. 2007-1217

Appeal from the Ohio
Board of Tax Appeals

BTA Case No. 2005-M-1069



APPELLANT ANCHOR LYONS LIMITED PARTNERSHIP BRIEF

Nicholas M.J. Ray (0068664)
Jay P. Siegel (0067701)
Siegel Siegel Johnson & Jennings Co. LPA
3001 Bethel Road, Suite 208
Columbus, OH 43220
(614) 442-8885

Thomas J. Scheve (0011256)
Assistant Prosecuting Attorney
230 East Ninth Street
Suite 4000
Cincinnati, OH 45202
(513) 946-3040

Counsel for Appellant
Anchor Lyons Limited Partnership

Counsel for Appellee
Hon. Dusty Rhodes, Hamilton
County Auditor and Board of
Revision

David DiMuzio (0034428)
David C. DiMuzio, Inc.
1900 Krgoer Building
1014 Vine Street
Cincinnati, OH 45202
(513) 621-2888

Marc Dann (031514)
Ohio Attorney General
30 E. Broad Street
17th Floor
Columbus, OH 43215-3428
(614) 466-4320

Counsel for Appellee
Cincinnati School District
Board of Education

Counsel for Appellee
Richard A. Levin, Tax
Commissioner of Ohio

TABLE OF CONTENTS

TABLE OF AUTHORITIESiii

APPENDIXiv

INTRODUCTION1

STATEMENT OF THE CASE AND FACTS6

ARGUMENT IN SUPPORT OF PROPOSITIONS OF LAW9

I. The holding in *Berea City School Dist. Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision* (2005), 106 Ohio St.3d 269 is not applicable to this case as the *Berea* case addressed the acceptance of a sale price that was indicative of the value of the real estate in-exchange where the property was multi-tenant and not built-to-suit a tenant. In contrast, the instant matter concerns the sale of a single tenant property valued in-use, where the property was built to that tenant’s unique needs and the transfer is reflective of the business success and credit-worthiness of the tenant and is unrelated to the value of the underlying real estate..10

II. The adoption of the sale price of the subject property would result in an unlawful assessment in use of the subject property.12

III. To adopt the sale price as the value of the subject property, it would be inconsistent with this Court’s holding in *Higbee Co. v. Cuyahoga Cty. Bd. of Revision* (2006), 107 Ohio St. 3d 325, wherein this Court rejected evidence of value inextricably intertwined with the non-real estate business value of the tenant.27

IV. It would be inconsistent with prior decisions of this Court, including most recently *Strongsville Bd. of Edn v. Cuyahoga Cty. Bd. of Revision* (2007), 112 Ohio St. 3d 309, that rejected similar sale and leaseback transactions to accept the sale price of the subject property.31

V. The testimony of the appraisers concerning the facts and circumstances surrounding the transfer of the property, and the characterization of the transfer's unreliability as an indication of value, constitutes admissible, competent, and probative evidence before the BTA.34

VI. Adoption of the sale price in this case is inconsistent with Ohio law, succinctly stated by this Court in *Alliance Towers, Ltd. v. Stark Cty. Bd. of Revision* (1988), 37 Ohio St.3d 16, that it is the fee simple value of the property which is to be valued for real property tax purposes.37

VII. Mr. Lorms' appraisal of the subject property constitutes competent, probative evidence of the value of the subject property.39

VIII. The Auditor's appraisal by Ms. Ebert does not constitute competent, probative evidence of the value of the subject property.44

CONCLUSION48

CERTIFICATE OF SERVICE50

TABLE OF AUTHORITIES

CASES

<i>Alliance Towers, Ltd. v. Stark Cty. Bd. of Revision</i> (1988), 37 Ohio St.3d 16. .	10,37,38,39
<i>Berea City Schools v. Cuyahoga Cty. Bd. of Revision</i> (2005), 106 Ohio St. 3d 269.	<i>Passim</i>
<i>Bd. of Edn. of the Columbus City Schools v. Franklin Cty. Bd. of Revision</i> , (May 18, 2007), BTA Case Nos. 2005-R-329 and 330, unreported, <i>on appeal to the Ohio Supreme Court</i> docket number 2007-1086.....	3,24
<i>Cleveland Hts./Univ. Hts. Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision</i> (1995), 72 Ohio St. 3d 189.	32
<i>Dayton School Dist. Bd. of Edn. v. Montgomery Cty. Bd. of Revision</i> (September 2, 2005), BTA No. 2004-V-76, unreported.	13,28,29,31
<i>Higbee Co. v. Cuyahoga Cty. Bd. of Revision</i> (2006), 107 Ohio St. 3d 325.	<i>Passim</i>
<i>Kroger Co. v. Hamilton Cty. Bd. of Revision</i> (1993), 67 Ohio St. 3d 145.	31,32,33
<i>Pingue v. Franklin Cty. Bd. of Revision</i> (1999), 87 Ohio St. 3d 62.	32
<i>Ratner v. Stark Cty. Bd. of Revision</i> (1988), 35 Ohio St.3d 26, 28.	10,11
<i>S. Euclid/Lyndhurst Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision</i> (1996), 74 Ohio St. 3d 314, 317.	31
<i>State ex rel. Park Inv. Co. v. Board of Tax Appeals</i> (1972), 32 Ohio St. 2d 28. ...	12,13,20
<i>Strongsville Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision</i> (2007), 112 Ohio St. 3d 309.	2,10,31,32,33,34
<i>Worthington City Schools v. ABCO Insulation</i> (1992), 84 Ohio App. 3d 144, 152	36
<i>Zazworsky v. Licking Cty. Bd. of Revision</i> (1991), 61 Ohio St. 3d 604, 605-606.	10

OTHER

1972 Notes to Evid. R. 703	36
Evid. R. 602	35
Evid. R. 703	35,36
<i>The Appraisal of Real Estate</i> , 12 th Edition.	2,4,5,14,25
Article XII, Section 2, <i>Ohio Constitution</i>	1

APPENDIX

Notice of Appeal from the Ohio Board of Tax Appeals to Ohio Supreme Court.....	1
Ohio Board of Tax Appeals Decision and Order.....	13
Franklin County Board of Revision Decision.....	25
<i>Bd. of Edn. of Berea City School Dist. v. Cuyahoga Cty. Bd. of Revision</i> , (July 14, 2006) BTA Nos. 2002-V-2595 & 2002-V-2800, unreported.....	26
<i>Bd. of Edn. of the Columbus City Schools v. Franklin Cty. Bd. of Revision</i> , (May 18, 2007), BTA Case Nos. 2005-R-329 and 330, unreported, <i>on appeal to the Ohio Supreme Court</i> docket number 2007-1086.....	38
<i>Dayton School Dist. Bd. of Edn. v. Montgomery Cty. Bd. of Revision</i> (September 2, 2005), BTA No. 2004-V-76.....	50
<i>Schottenstein v. Bd. of Revision of Franklin Cty.</i> (Dec. 29, 1977), Franklin App. Nos. 77AP-713 and 77AP-714, unreported [available on Westlaw; 1977 WL 200712].	69
<i>Zell v. Franklin Cty. Bd. of Revision</i> (Aug. 26, 1986), Franklin App. No. 86AP-153, unreported [available on Westlaw; 1986 WL 9522].	72
Amendment XIV, Section 1, <i>United States Constitution</i>	75
Article XII, Section 2, <i>Ohio Constitution</i>	76
<i>The Appraisal of Real Estate</i> , 12 th Edition, pages 24-25	78
<i>The Appraisal of Real Estate</i> , 12 th Edition, pages 38-39	80
<i>The Appraisal of Real Estate</i> , 12 th Edition, pages 81-82	82
<i>The Appraisal of Real Estate</i> , 12 th Edition, page 350	84

INTRODUCTION

The subject property was designed and built-to-suit specifically for use by Wal-Mart. Wal-Mart outsourced the development of the property. Rather than utilizing mortgage loan financing to pay off the costs of constructing the store, Wal-Mart instead entered into a long term lease with the developer to amortize the construction costs in lieu of a mortgage. The lease did not reflect the market value of the improvements, as many of the design requirements of the store were unique to the needs of Wal-Mart. Rather, the lease reflected the value of the property to Wal-Mart as the user. In terms of valuing property, this is referred to as valuing in use. This value in use lease based on construction costs in turn formed the basis of a subsequent sale by the developer to an investor. The value-in-use lease based on construction costs carried the guarantee of payment by one of the most highly successful, credit-worthy tenants in the country—Wal-Mart. The County Auditor’s and Property Owner’s appraisers agree that the sale price was driven significantly, if not totally, by the value-in-use lease and the business success and credit-worthiness of Wal-Mart as the tenant guaranteeing payment.

The taxation of real property in Ohio was founded in and has stressed that “[I]and and improvements thereon shall be taxed by uniform rule according to value.” Ohio Const. Art. XII, § 2. Recently, the principle of uniform taxation without regard to who owns or occupies the building was reaffirmed by this court in *Higbee Co. v. Cuyahoga Cty. Bd. of Revision* (2006), 107 Ohio St. 3d 325, wherein the Ohio Supreme Court rejected evidence of value inextricably intertwined with the non-real estate business value of the tenant. A blind application of this court’s decision in *Berea City School Dist. Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision* (2005), 106 Ohio St.3d 269 without further analysis of the transaction and where the decision is distinguishable from the facts in this case would result in an unconstitutional, non-uniform

assessment of real property in Ohio. As this court recently commented in *Strongsville Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision* (2007), 112 Ohio St. 3d 309, this court's *Berea* decision contemplates an analysis of the transaction and not blind acceptance of a sale price. Such an analysis in this case, supported by market evidence and expert testimony, proves that the sale price does not reflect only the value of the real property and the decision of the Ohio Board of Tax Appeals blindly accepting such a value without deeper analysis of the fundamentals surrounding the transaction must be over turned.

While the issues in this case concern the assessment of a single-tenant commercial property designed and built specifically for Wal-Mart, the principles are not altogether different than those faced by the typical homeowner. Does the cost of building a home always equal its value? What if the homeowner had unique tastes, perhaps wanted stained glass in the family room, wheelchair access for a disabled family member, solar panels to generate electricity or a wine cellar dug into the basement? While most of the home would probably maintain its value, it is quite possible that a subsequent buyer of that property might not place equal value on the stained glass, wheelchair access, solar electricity or wine cellar. So the home would have one value to the user it was designed for, perhaps reflected in their costs of construction, but likely an altogether different value to another user/buyer when it came time to sell the property. This valuation distinction is addressed by *The Appraisal of Real Estate*, 12th Edition, pp. 24-25, and illustrates the important difference between the value of a property to a user in contrast to the fair market value to others on the open market.

These are some of the exact same issues to be addressed in the instant case. It is important to consider this transaction not in a vacuum, but in the context of the market as a whole. To believe that it is probable that the sale of the subject property, as a function of its value-in-use lease,

further driven by the business success and creditworthiness of Wal-Mart as lessee, is equal to the value of the underlying real estate, one would have to believe many other verifiably implausible propositions, including the following:

- Is it probable that a 15,000 square foot retail building on Kenny Road in Columbus, just north of Upper Arlington, is worth the same or less than an almost identical building on South High Street in South Columbus? (Appellant's Supplement, p. 138; Lorms,¹ p. 55). No, a property on Kenny Road is not equal in value to an identical property on South High Street. For further review of this exact situation, see Sales Comparison 1 on page 21 of Appellant's Brief.
- Is it probable that a ten year old 150,000 square foot retail storeroom on Brice Road in Columbus is worth twice as much as a nearly identical building in Mill Run in Hilliard? (Appellant's Supplement, p. 136; Lorms, p. 53). No, a nearly identical property on Brice Road in Columbus is not worth twice as much as a property in Mill Run in Hilliard. For further discussion of this exact situation, see Sales Comparison 2 on page 22 of Appellant's Brief.
- Is it probable that a Walgreens drugstore at the intersection of Demorest and Clime Roads in Columbus is worth 30% more than a CVS drugstore **at the same intersection?** (see *Board of Edn. of the Columbus City Schools v. Franklin Cty. Bd. of Revision* (May 18, 2007), BTA Case Nos. 2005-R-329 and 330, unreported, *on appeal to the Ohio Supreme Court* docket number 2007-1086.) No, a similar drugstore at the same intersection would not be worth 30% more than the other. For further discussion of this exact situation, see Sales Comparison 3 on page 24 of Appellant's Brief.

¹ The appraisal report prepared by Robin Lorms and admitted into evidence as Appellee's Exhibit 1 before the Ohio Board of Tax Appeals will hereafter be cited as "Lorms, p. ___".

- Is it probable that a storeroom leased by Kmart, recently out of bankruptcy, identical in every way to a Wal-Mart storeroom right next door, under the exact same lease terms, would sell on the open market for the same amount? No, the business success and creditworthiness of Wal-Mart would result in investors being willing to pay more for the Wal-Mart property. This is in contradiction to the guidance from this Court in *Higbee* stating that the properties should be similarly valued. For further discussion of this, see the discussion of *Higbee* beginning on page 27 of Appellant's Brief.
- Is it probable that a building designed specifically for the unique needs of one user is equally valuable to another user with different needs? No, the property was specifically built to meet the unique needs of one user and is valuable to that user. That value, however, is not shared by another user without the same unique needs. *The Appraisal of Real Estate*, 12th Edition, pg. 25. See the value-in-use discussion being on page 12 of Appellant's Brief.
- Is it probable that when a build-to-suit, single tenant property encumbered by a value in use lease entered into with an investment-grade tenant as a result of the tenant's business success and creditworthiness sells it is similar, in any meaningful way, to the sale of a multi-tenant property, not designed for a single user, without a value in-use lease or a purchase price driven by the business success and creditworthiness of the multiple tenants? No, there is no similarity between these transactions. The first transaction is the one, the Auditor argues in this case, that should be relied upon to value the real property component of the subject property before the Court while the second transaction was at issue in *Berea City Schools v. Cuyahoga Cty. Bd. of Revision* (2005), 106 Ohio St. 3d 269. See the detailed discussion of *Berea*, beginning on page 10 of Appellant's Brief.

- Is it probable that a rational buyer would pay more for real estate than the cost to build and replace the same real estate? In other words, would a rational buyer pay almost \$16,000,000 for real estate if the same buyer could build a brand new identical property for \$11,600,000 or 13,500,000—depending upon which expert’s opinion of land value is used? No, no rational buyer would pay more for a property than the cost to replicate an identical new property. Such a conclusion is consistent with the Principle of Substitution set forth in *The Appraisal of Real Estate*, 12th Edition, pp. 38-39. See the discussion of the Principle of Substitution beginning on page 25 of Appellant’s Brief.
- Is it probable that the auditor's own appraiser's admission that the purchase of the subject property was driven by the business success and creditworthiness of the tenant was false? No, such an opinion is correct. It is not the appraiser’s role to understand that this Court’s holding in *Higbee* was that the business success of the tenant shall not impact the real property value for taxation purposes. See the further discussion of *Higbee* beginning on page 27 of Appellant’s Brief.
- Is it probable that in addition to all of the other taxes imposed on businesses in Ohio that are directly correlated to their success, the legislature intended that the assessment of real estate taxes should also impose additional taxes on real estate users as a function of the success of the user's business? No, the real property tax is not a tax tied to the business success of the activities conducted on or in the property but rather of the property itself. Such is the holding of this Court in *Higbee*. See the further discussion of *Higbee* beginning on page 27 of Appellant’s Brief.

The probability that any of the above propositions are true is almost non-existent. The sale relied upon by the Auditor and the BTA is as a result of the market described above and

reflects the business success and creditworthiness of a lessee in a build-to-suit, value in use lease. It does not only reflect the value of the real property. In the instant matter, the original lease of the subject property reflects the costs of construction and the use-value to the tenant the property was designed for. The subsequent sale of the property, subject to the value-in-use lease by Wal-Mart, a highly successful and credit-worthy tenant, also reflects the use-value of the property. Furthermore, reliance on *Berea City School Dist. Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision* (2005), 106 Ohio St.3d 269 in arguing that the sale is the best evidence of value is misplaced, as the facts and circumstances of this case more closely reflect this Court's mandate in *Higbee Co. v. Cuyahoga Cty. Bd. of Revision* (2006), 107 Ohio St. 3d 325 that assessment of Ohio real property must disregard evidence concerning the success of the tenant's business and the value of the property to a specific user.

STATEMENT OF THE CASE AND FACTS

The subject property is designated by the Hamilton County Auditor as permanent parcel number 248-0002-0033-00. (Appellant's Supplement, p. 84; Lorms, p. 1). The property is located at 2322 Ferguson Road in Cincinnati. (Appellant's Supplement, p. 84; Lorms, p. 1). The subject has a total land area of 14.006 acres. (Appellant's Supplement, p. 84; Lorms, p. 1). The site was improved in 1996 with a one-story, 148,925 square foot discount retail storeroom. (Appellant's Supplement, p. 84; Lorms, p. 1).

The subject property was designed and constructed by a third party developer in accordance with the demands and unique business needs of a specific user, in this case Wal-Mart. (Appellant's Supplement, p. 86; Lorms, p. 3). This process of development is frequently referred to as building a property to suit the user. As is the common practice with these "build-to-suit" properties, the developer secured a net lease from Wal-Mart after the completion of

construction based on the amortized cost of constructing the property. (Appellant's Supplement, p. 86; Lorms, p. 3). (A copy of the complete lease begins on page 335 of Appellant's Supplement.) The developer then sold the property with the lease in place in what is commonly referred to as the net lease market. As will be discussed below, the sale price obtained for the property reflected the value of the property to Wal-Mart in use. (Appellant's Supplement, p. 86; Lorms, p. 3). In other words, the sale price reflected "value-in-use" rather than "value-in-exchange" and therefore an assessment of the property based on its sale price in the net lease market would result in a use-value assessment prohibited by the law in Ohio. As will also be discussed at some length below, the case *Berea City School Dist. Bd. of Edn. v. Cuyahoga Cty. Bd.* (2005), 106 Ohio St. 3d 269 does not apply because, unlike the instant case, *Berea* involved a sale reflecting "value-in-exchange" in the normal real estate market.

The main retail artery near the subject property is Glenway Crossings. Glenway near the subject is not proximate to any highway interchange. (Appellant's Supplement, p. 36; Transcript², pp. 134-136). Off of the main Glenway artery is a connecting artery Glenhills, which then connects to Ferguson Road. (Appellant's Supplement, p. 36; Tr., pp. 134-136). The subject property only has 46 feet of frontage along Ferguson, which is itself isolated from the primary retail traffic along Glenway. (Appellant's Supplement, p. 36; Tr., pp. 134-136). In fact, because of its remote location, Wal-Mart actually had to erect a billboard off of Glenway directing traffic to where it is located. (Appellant's Supplement, p. 36; Tr., pp. 134-136).

Demographically, the subject is also inferior in many respects. The median income in the surrounding trade area is \$50,327, compared with the average in Cincinnati of \$68,684. (Appellant's Supplement, p. 101; Lorms, p. 18). And while the population is dense, it also has been declining for many years. Between 1990 and 2000, while the Cincinnati population was

² The Transcript of Hearing before the BTA on September 8, 2006 will hereafter be cited as "Tr., p. ___".

increasing by 8.93%, the area around the subject suffered a decline in population of 4.45%. (Appellant's Supplement, p. 101; Lorms, p. 18). Similarly, between 2000 and 2005, the area population declined by an additional 5.86%, while Cincinnati's population continued to increase by 3.24%. (Appellant's Supplement, p. 101; Lorms, p. 18). Similar projections exist for the next five years. (Appellant's Supplement, p. 101; Lorms, p. 18).

For the tax year 2004, the Hamilton County Auditor ("Auditor") placed an assessed taxable value on the subject parcel of \$3,252,690, equating to a fair market value of \$9,293,400. On March 30, 2005, the Cincinnati School District Board of Education ("School Board") filed a complaint with the Hamilton County Board of Revision ("BOR") seeking to increase the assessment of the parcel to \$5,571,600 or a total market value of \$15,918,915. The basis of the increase being sought by the School Board was a sale of the subject parcel on October 7, 2004.

On July 26, 2005, the Hamilton County Board of Revision held a hearing concerning the School Board's complaint. The School Board offered as evidence a conveyance fee statement purporting to establish a sale of the subject property as the best evidence of value. The Taxpayer rebutted the School Board's evidence with a rental survey, a copy of the lease encumbering the subject property, and expert opinion of Robin Lorms, MAI, of Integra Realty Resources – Columbus. On August 1, 2005, the BOR issued its decisions maintaining the Auditor's original value.

The School Board then appealed to the Ohio Board of Tax Appeals ("BTA") on August 19, 2005. The case was assigned to Attorney Examiner Rebecca Luck. After the parties had an opportunity to conduct discovery, the case proceeded to hearing before the BTA on September 8, 2006. Once again, the School Board relied on the conveyance fee statement in support of its claimed value. The Auditor relied on an appraisal prepared by Antoinette Ebert, staff appraiser

for the Hamilton County Auditor's office. Ms. Ebert testified that she believed that value of the subject property was consistent with its sale price.³

In addition to the statutory transcript from the Board of Revision, which contained, among other things, the build-to-suit lease that encumbered the subject property at the time of its sale, the Taxpayer offered the appraisal and testimony of Robin Lorms at the BTA hearing. Mr. Lorms outlined various reasons why the sale price was not reflective of value, and how it primarily reflected the use value of the property instead of its value in exchange. Mr. Lorms further supported his opinion with an independent appraisal of the subject property for \$6,000,000. (Appellant's Supplement, p. 173; Lorms, p. 90).

On June 8, 2007, the BTA reversed the BOR's decision and determined that the sale price was the best evidence of value. The Property Owner's appeal from the BTA decision is now before this Court.

ARGUMENT IN SUPPORT OF PROPOSITIONS OF LAW

The Property Owner will establish, by clear and convincing evidence submitted in the record, the following:

- I. The holding in *Berea City School Dist. Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision* (2005), 106 Ohio St.3d 269, is not applicable to this case as the *Berea* case addressed the acceptance of a sale price that was indicative of the value of the real estate in-exchange where the property was multi-tenant and not built-to-suit a particular tenant. In contrast, the instant matter concerns the sale of a single tenant property valued in-use, where the property was built to that tenant's unique needs and the transfer is reflective of the business success and credit-worthiness of the tenant and is unrelated to the value of the underlying real estate.
- II. Adoption of the sale price of the subject property would result in an unlawful assessment in use.

³ The appraisal report prepared by Antoinette Ebert and admitted into evidence as Appellant's Exhibit A before the Ohio Board of Tax Appeals will hereafter be cited as "Ebert, p. ___".

- III. To adopt the sale price as the value of the subject property, it would be inconsistent with this Court's holding in *Higbee Co. v. Cuyahoga Cty. Bd. of Revision* (2006), 107 Ohio St. 3d 325, wherein this Court rejected evidence of value inextricably intertwined with the non-real estate business value of the tenant.
- IV. Accepting the sale price as the property's value is inconsistent with prior decisions of this Court, including most recently *Strongsville Bd. of Edn v. Cuyahoga Cty. Bd. of Revision* (2007), 112 Ohio St. 3d 309 that rejected similar sale and leaseback transactions.
- V. The testimony of the appraisers concerning the facts and circumstances surrounding the transfer of the property, and the characterization of the transfer's unreliability as an indication of value, constitutes admissible, competent, and probative evidence before the BTA.
- VI. Adoption of the sale price in this case is inconsistent with Ohio law, succinctly stated by this Court in *Alliance Towers, Ltd. v. Stark Cty. Bd. of Revision* (1988), 37 Ohio St.3d 16, that it is the fee simple value of the property which is to be valued for real property tax purposes.
- VII. The appraisal of the subject property by the Property Owner's expert constitutes competent, probative evidence of its value.
- VIII. The appraisal of the subject property by the Auditor's witness does not constitute competent, probative evidence of its value.
- I. **The holding in *Berea City School Dist. Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision* (2005), 106 Ohio St.3d 269 is not applicable to this case as the *Berea* case addressed the acceptance of a sale price that was indicative of the value of the real estate in-exchange where the property was multi-tenant and not built-to-suit a tenant. In contrast, the instant matter concerns the sale of a single tenant property valued in-use, where the property was built to that tenant's unique needs and the transfer is reflective of the business success and credit-worthiness of the tenant and is unrelated to the value of the underlying real estate.⁴**

In the instant matter, the Auditor is relying on a sale to argue for the valuation of the subject property. In *Zazworsky v. Licking Cty. Bd. of Revision* (1991), 61 Ohio St. 3d 604, 605-606, this Court, quoting *Ratner v. Stark Cty. Bd. of Revision* (1988), 35 Ohio St.3d 26, 28, stated: "[A]lthough the actual sale price provides strong evidence of market value other factors can

⁴ This Proposition of Law addresses Assignments of Error 10, 16 and 21.

affect the use of the sale price of property as evidence of its true value. These factors might include the mode of payment, sale-lease arrangements, [or] abnormal economic conditions.” While this Court overturned *Ratner* in *Berea, supra*, it only did so in part, specifically as it relates to a sale where the price incorporated favorable financing. Consideration of “other factors” showing that the sale is not indicative of value remains subject to review.

The Auditor and the BTA in its decision place great reliance on *Berea*. What is beyond dispute, however, is the substantial factual difference between *Berea* and the instant matter. In the instant matter, as will be explained below, the sale of the subject property, subject to a build-to-suit, value-in-use, net lease, reflects the value of the property in use to a specific tenant. In contrast, the *Berea* sale price reflected the property’s value in exchange and, absent evidence indicating otherwise, the Court adopted the sale price. The issue of whether the adoption of the sale price would reflect the use-value of the *Berea* property was not raised. Unlike the instant case, there was no evidence in *Berea* that the property in that case was subject to a built-to-suit, value-in-use lease that later formed the basis for the sale of the property in the net lease market. In fact, the *Berea* property had three tenants, Kmart, Lentine’s, and Burger King, which would clearly be inconsistent with the idea that it was functional or built-to-suit for only one user, as is the case with the subject property. Furthermore, there was no evidence that the sale price in *Berea* was a function of the business success and credit-worthiness of the tenants. Because the *Berea* property was not sold subject to a value-in-use lease designed to amortize the costs of construction, the sale of the property reflected its value in exchange, not its value in use.

Conversely, as will be discussed below, the instant sale is clearly reflective of the subject property’s use-value, driven by the build-to-suit, value-in-use lease encumbering the property as well as the credit-worthiness of Wal-Mart as a tenant. Accordingly, the *Berea* decision is

inapposite and does not answer the issues raised in the instant appeal. Indeed, this Court's decision in *Higbee* addresses the facts and circumstances in the instant appeal and mandates that the sale of the subject property not be relied upon as an indication of value.

Finally, it should be emphasized that the exception to *Berea* at issue in this case is extremely narrow. Those properties that are single tenant are an extremely small component of the overall market for commercial real estate. Furthermore, not all single tenant commercial properties are designed specifically for a user, with a lease to amortize construction costs, and then sold pursuant to that lease in further reliance on the success and credit-worthiness of the tenant. As such, the exception to *Berea* urged by the Property Owner would apply to a very limited number of properties.

II. The adoption of the sale price of the subject property would result in an unlawful assessment in use of the subject property.⁵

The sale price of the subject property represents its value-in-use. (Appellant's Supplement, p. 86; Lorms, p. 3; see also, Appellant's Supplement, pp. 129-139; Lorms, pp. 46-56). This Court has consistently ruled that the Ohio Constitution prohibits the adoption of the use-value of real estate for assessment purposes. In *State ex rel. Park Inv. Co. v. Board of Tax Appeals* (1972), 32 Ohio St. 2d 28, this Court stated as follows:

* * * We have held that Section 2, Article XII of the Ohio Constitution and the Fourteenth Amendment to the United States Constitution require that the ultimate result of an appraisal must be to determine that amount which the property should bring if sold on the open market. *State ex rel. Park Invest. Co., v. Bd. of Tax Appeals, supra* (175 Ohio St. 410, 412); *State ex rel. Park Invest. Co., v. Bd. of Tax Appeals, supra* (26 Ohio St. 2d 161, 167).

* * *

Since the **current use** method of evaluation excludes, among other factors, location and speculative value which comprise market

⁵ This Proposition of Law addresses Assignments of Error 2, 3, 4, 5, 6, 7, 11, 13, 14, 15, 16, 19, 20 and 22.

value, such **current use** method cannot be made the basis for valuation of real property for tax assessment purposes, and that portion of [the statute] making provision for such method of valuation is invalid, as being contrary to Section 2, Article XII of the Ohio Constitution, which enjoins that land and improvements thereon shall be taxed by uniform rule according to value. (Emphasis added.)

Consistent with the above holding of this Court, in a case virtually identical to the instant matter, the BTA recently held that the sale of a drugstore subject to a build-to-suit lease was, in fact, indicative of its value in use. In *Dayton School Dist. Bd. of Edn. v. Montgomery Cty. Bd. of Revision* (September 2, 2005), BTA No. 2004-V-76, unreported, the BTA had the opportunity to address the exact same questions that are at issue in the instant matter and concluded that the sale price of a build-to-suit, single tenant retail property is a function of the tenant's credit-worthiness and an indication of the use-value of the property. Just weeks before this Court issued its decision in *Berea*, the BTA rejected an appraiser's reliance on sales of drug stores that were built-to-suit, stating the following:

Nevertheless, [the BOE's appraiser's] opinion of value is borne from his exclusive reliance on the sixteen similar build-to-suit comparables, all of which present the same issues concerning the occupants' credit-worthiness and the like. The data gleaned from the comparables appear to be tied (as is in the case of the subject) to the credit-worthiness of their tenants. The difficulty in relying upon income derived from a business activity, or **value in use**, is that the value ultimately derived may not be the market value of the subject property. (Emphasis added)

The decision in *Dayton* was, in part, a factual determination of the nature of single-tenant, net leased sales that is indistinguishable from the factual question that is being raised in the instant appeal. The BTA in *Dayton* properly recognized the prohibition against use-value assessments articulated by this Court in *State ex rel. Park Inv. Co. and Higbee*. Obviously, the

BTA in the instant matter only now felt erroneously constrained by this Court's *Berea* decision in adopting a sale that the BTA clearly believes reflects its value-in-use.

As discussed above, none of the questions relating to use-value and the non-real estate value of the tenant's credit-worthiness were at issue in *Berea*, unlike the instant case. The evidence in the instant record, which has not been impeached or rebutted in any way, and is supported by appraisal theory, law, expert testimony, and data from market transactions, indicates that the adoption of the sale price would result in a prohibited use-assessment of the subject property.

To understand how the transaction in this case represents the use-value of the subject property, it is necessary to review the theoretical and logical underpinnings of the notion that the sale of the subject property is indicative of its use-value. The best way to examine the concept of use-value is to consider the often cited example of a hypothetical manufacturer with a unique manufacturing process. As discussed in *The Appraisal of Real Estate* on page 25 and in Mr. Lorms' appraisal beginning on page 46 (Appellant's Supplement, p.129), the hypothetical manufacturer's property might have a use-value to the manufacturer for which it was designed and built in order to maximize the utility of their business enterprise. If the same building was placed on the open market, however, and other manufacturers that did not utilize the same manufacturing process were to purchase it, it would have a different, lesser value in exchange.⁶

The value-in-use to the manufacturer that designed the manufacturing property and had it built-to-suit its business enterprise cannot be the basis of the assessment of the property under Ohio law. To see how this prohibited result might occur if a transfer value is blindly utilized to

⁶ The value in exchange need not necessarily be less than the value in use. Specifically, in Ohio, agriculture property is valued under the state's Certified Agricultural Use Valuation ("CAUV") program. The program is necessary because property is otherwise valued in exchange in Ohio. In contrast with the manufacturing property example and the subject property before this Board, the values of properties in use for agriculture are usually less than their value in exchange.

value property in Ohio, one first needs to consider how the occupancy by the hypothetical manufacturer might be accomplished.

If the manufacturer decides to own its facility, it could buy the land, hire an architect and contractor, and have the facility constructed to its specifications. (Appellant's Supplement, pp. 129-130; Lorms, pp. 46-47). After it is built, the manufacturer can take out a mortgage to amortize the costs of the land and building. Many businesses, however, rather than investing in ownership of their real estate, can earn higher returns on their capital in their core business. (Appellant's Supplement, p. 129; Lorms, p. 46). Therefore, these users prefer to lease their real estate. Again, returning to the hypothetical manufacturer, if it decides to lease its real estate, it can do so either via a sale/leaseback arrangement or by simply entering into a lease with a third party developer who is hired to construct the property for the manufacturer. As Mr. Lorms stated,

[W]hether the user designs, builds and owns their own facility; designs, builds and enters into a sale/leaseback transaction; or, enters into a build-to-suit lease agreement with a developer, the development costs, sale price or lease rates are driven by the value in use to the business enterprise. (Appellant's Supplement, p. 131; Lorms, p. 48).

The resulting lease is a function of the costs to develop the property. (Appellant's Supplement, p. 130; Lorms, p. 47). In turn, the costs to develop the property are a function of the specific and unique needs of the manufacturer's business enterprise. (Appellant's Supplement, pp. 129-130; Lorms, pp. 46-47). The obsolescence that may be inherent in the design to other manufacturers is not reflected in the build-to-suit lease. (Appellant's Supplement, p. 39; Tr., pp. 146-147). Therefore, the lease reflects the property value to the user, or value-in-use, not its market value or value in exchange. (Appellant's Supplement, p. 130; Lorms, p. 47). Similarly, any subsequent sale based upon that value-in-use lease is a reflection

of the value of the property in-use, not in-exchange. (Appellant's Supplement, p. 130; Lorms, p. 47).

Although the foregoing example concerns the development of a manufacturing facility that has different value-in-use and value-in-exchange, the same principles apply to other property types as well. Whereas a manufacturer might have a floor-plan unique to its business enterprise, including specific square footage requirements, ceiling heights, loading docks, construction materials, and layout, so too may a retailer. (Appellant's Supplement, pp. 130-131; Lorms, pp. 47-48). Many retailers have floor-plans and requirements that are equally unique to their business enterprise. (Appellant's Supplement, p. 39; Tr., p. 148; Appellant's Supplement, p. 130-131; Lorms, pp. 47-48).

Indeed, evidence that these specific design requirements differ from user to user can be found in the fact that single-tenant retail properties are almost always built-to-suit for the user. (Appellant's Supplement, p. 103; Lorms, p. 20). If these design requirements were readily interchangeable, these stores would be built speculatively and held on the open market for sale or lease to the highest bidding user. This, however, is not the manner in which these stores are developed, as big box discount storerooms are never built on a speculative basis. (Appellant's Supplement, p. 103; Lorms, p. 20).

As Lorms states,

The most obvious example of the lack of utility of an existing big box on the open market is provided by two brand new big boxes in the Columbus market area. These two stores were constructed by an area developer for occupancy by Ames. Before Ames took occupancy, they went into bankruptcy and vacated all of their stores in Ohio. Thus, two brand new, never occupied big boxes were available on the open market. One was located in an in-filled market area with high population density across from a new Lowe's store. The other was located at the corner of an interchange along a dynamic retail corridor that included a recently

constructed Kroger anchored shopping center and a proposed Wal-Mart supercenter. The Wal-Mart supercenter was constructed across the street from the [former Ames] property. Thus, the [former Ames] property was given no interest by Wal-Mart. Both [Ames] properties were on the market for approximately three to four years before the developer settled on interested parties, Target and Home Depot. Both retailers purchased the properties and demolished the brand new existing improvements for construction of their own store prototypes, even though they were of similar size. This provides evidence that vacant big boxes hold little or no value for the national retailers. (Appellant's Supplement, p. 105; Lorms, p. 22).

Obviously, if, prior to the bankruptcy of Ames, Ames had entered into leases with the developer designed to amortize the construction costs, and the Ames properties sold subject to the build-to-suit, value-in-use leases, the obsolescence that was subsequently borne out by the market when Target and Home Depot demolished both brand new stores would not have been reflected in the net lease sales of the Ames properties. Similarly, in the case of the subject property, whatever obsolescence is inherent in the Wal-Mart improvements is not reflected in the purchase price of the subject property when it is sold subject to a Wal-Mart build-to-suit lease that reflects the value of the property only to Wal-Mart, not the rest of the market in exchange.

As Lorms explained:

Where a building is designed and constructed to meet the user's specific needs, regardless of whether the ultimate transaction results in the user leasing the new building, purchasing it from the developer, or building it itself and then selling to an investor (sale/leaseback), the final outcome is identical – a financial transaction to accommodate the value-in-use by the specific user. The value reflected by that transaction is unique to that specific user and not, in and of itself, reflective of the market value or value in exchange of the property.” (Appellant's Supplement, p. 132; Lorms, p. 49).

PROPERTIES SUBJECT TO A VALUE-IN-USE LEASE ARE SOLD IN THE NET LEASE MARKET, NOT THE OPEN REAL ESTATE MARKET

After a user has a building built-to-suit, and executes a value-in-use lease with its developer to amortize the construction costs, the property will typically be sold to a third party in what is commonly referred to as the net lease market as opposed to the traditional real estate market. (Appellant's Supplement, p. 40; Tr., p. 150). In the net lease market, single tenant properties with high credit tenants and long term leases are sold to investors. (Appellant's Supplement, pp. 40-42; Tr., pp. 150-157). As explained below, a sale of the property in this market is determined based on the value-in-use lease and the credit-worthiness of the lessee without regard to the value-in-exchange of the real estate, and therefore is not indicative of the market value of the property.

Many characteristics of the net lease market distinguish it from the typical real estate market. First, the typical buyer is frequently from out of town, has limited knowledge of local real estate market dynamics, and may not even personally see the property before purchasing it. (Appellant's Supplement, pp. 40-42; Tr., pp. 150-157; Appellant's Supplement, pp. 86-87; Lorms, pp. 3-4). Such buyers base their purchase decisions on the value-in-use lease and the credit-worthiness of the tenant, without regard to the value of the real estate itself. (Appellant's Supplement, pp. 40-42; Tr., pp. 150-157; Appellant's Supplement, pp. 86-87; Lorms, pp. 3-4). In contrast, the typical purchaser in the traditional real estate market is much more knowledgeable about the local market, is motivated by typical real estate fundamentals such as location and certainly would be unlikely to purchase a property without ever seeing it. (Appellant's Supplement, p. 87; Lorms, p. 4).

Second, the financing of net lease transactions is quite different from other real estate transactions. (Appellant's Supplement, p. 41; Tr., pp. 155-156). Whereas in the average real estate transaction the lender will require debt service coverage of 1.2 to 1.3 times the net income generated by the property, the debt service coverage required from a buyer of a net leased property is only 1.003. (Appellant's Supplement, pp. 224-263; Lorms, Addendum G). The low debt service rate allows for buyers to pay higher prices and produce lower down payments in net lease transactions. Indeed, when the spread between net lease payments of the user/tenant and the debt service of the buyer is only 0.003, it suggests that the lessee, for all intents and purposes, stands in the shoes of the borrower/buyer. For all but the slimmest amount, it is the lease payment of the lessee servicing the entire debt on the property. This suggests that the build-to-suit net lease transactions, unlike sales in the traditional real estate market, are nothing more than financing mechanisms for the user. (Appellant's Supplement, p. 103; Lorms, p. 20).

Third, unlike traditional real estate investments such as apartment buildings, office buildings, or shopping centers, which require active professional management for the investment to succeed, the ownership of net-leased property is completely passive. (Appellant's Supplement, p. 136; Lorms, p. 53). A transaction involving net-leased property, with passive income based upon the credit-worthiness of the tenant, is much more akin to a financial or bond transaction than a real estate transaction. (Appellant's Supplement, p. 136; Lorms, p. 44).

Fourth, much like the financial markets, net-leased properties are much more liquid than other types of investments in real estate. (Appellant's Supplement, pp. 135-136; Lorms, pp. 52-53). Whereas the typical real estate transaction is culminated only after extensive time, effort, and due diligence, the net-leased properties are bought and sold over the internet, often sight unseen. (Appellant's Supplement, p. 136; Lorms, p. 53). If it becomes necessary for the

property to again be sold, it can again be listed on the internet and quickly sold, unlike a traditional real estate sale.

In summary, the value-in-use lease, which reflects the cost to construct the property to the specific requirements of the user's business enterprise, is the basis of the value-in-use sale price in the net-lease market. The net-lease market has many characteristics that distinguish it from traditional real estate markets, including (1) purchase prices driven by the value-in-use lease and the credit-worthiness of the tenant without regard to the market value of the real estate being purchased, (2) different debt service requirements, (3) passive ownership with no need for any professional management in order to maintain the value of the investment, and (4) much greater liquidity. As such, the sale price of a net leased property in the net lease market does not reflect the value of the underlying real property in the normal real estate market, i.e. its value-in-exchange. Therefore, an assessment of the property based on the sale price in the net lease market is prohibited by Ohio law. *State ex rel. Park Inv. Co., supra.*

As Mr. Lorms concludes:

[U]sing net-leased comparable sales in a fee simple valuation is not appropriate because they do not account for the normal risk and return factors in a given market that would influence rents and occupancy. Only fee simple sale comparables will reflect the relevant market norms in the areas of financing, market dynamics, capitalization rates, liquidity, ownership and management. . . . Comparing net-leased sale or lease data to a fee simple property is like comparing apples to oranges. (Appellant's Supplement, p. 136; Lorms, p. 53).

MARKET EVIDENCE REFLECTS THE DISTINCTION BETWEEN VALUE-IN-USE AND MARKET VALUE

Based upon the foregoing, one would expect to find evidence of transactions in the market showing a lack of correlation between value-in-use net lease sale prices and the values of the underlying real estate. Such evidence is abundant. Consider the value-in-use net lease sales

of various Walgreens drugstores in greater Columbus presented in Mr. Lorms' report. The comparison between the Walgreens on Kenny Road and the Walgreens on South High Street is but one of many that illustrates the lack of any relationship to the underlying real estate.

<p align="center">Sale Comparison 1 (A superior location on Kenny Rd. sells for less than an inferior location in South Columbus)</p>						
Property	Year Built	Sale Date	GLA ⁷ (Square feet)	Price Per Square Foot	Population Household Income Housing Value	OAR ⁸
Walgreens 4540 Kenny Rd. Columbus, Ohio	2005	12/05	14,820	\$367.85	24,961 \$70,218 \$181,130	6.25%
Walgreens 3445 S. High St. Columbus, Ohio	2003	11/04	14,560	\$376.48	13,207 \$49,249 \$90,666	6.25%

(Appellant's Supplement, p. 138; Lorms, p. 55).

It seems unimaginable that a property on South High Street is equal in value to an identical property on Kenny Road. **In fact, the Kenny Road property actually sold for less.** Despite the fact that the Kenny Road property is newer, in a far superior location, with an 89% greater population, 43% greater income levels, and over twice the housing values, the South High Street property sold for slightly more. This cannot reasonably be explained on the basis of the underlying real estate fundamentals. Rather, it is strong evidence that the sale price in these transactions are determined by factors other than the real estate itself, such as the long term lease of a successful and credit-worthy tenant.

⁷ Gross Lease Area.

⁸ Overall Capitalization Rate.

Another example showing that value-in-use net lease sales are not correlated to the value of the real estate is the comparison between two big box sales in the greater Columbus area. Below are the characteristics of the Lowe's property on Brice Road, which sold subject to a value-in-use net lease, and the former Kmart in Mill Run, which sold unencumbered.⁹ As discussed above, this transaction also demonstrates the overwhelming difference between the sale price paid for a property subject to a build-to-suit, value-in-use lease, and the sale price paid for an unencumbered, fee simple interest.

<p align="center">Sale Comparison 2 (Demonstrating an inferior property sells for almost twice as much as a superior property due to a value-in-use net lease)</p>		
	<p align="center">Lowes's 2888 Brice Road Columbus, Ohio</p> <p align="center">(Net Lease, Value In Use Sale)</p>	<p align="center">Former Kmart 3780 Mill Run Columbus, Ohio</p> <p align="center">(Unencumbered Fee Simple Sale)</p>
Population (3-Mile Radius)	78,231	76,609
HH Income (3-Mile Radius)	\$55,594	\$88,655
Land Size	12.836 Acres	12.240 Acres
Building Size	125,357 SF	121,876 SF
Year Built	1995	1995
Sale Date	April-05	August-05
Sale Price	\$10,636,470	\$5,800,000
Price per SF	\$84.85	\$47.59

(Appellant's Supplement, p. 136; Lorms, p. 53).

⁹ Kmart was the former tenant, not the seller of the property.

Again, it seems unimaginable that a nearly identical property on Brice Road in Columbus, in an inferior market, is worth twice as much as a property in Mill Run in the Hilliard area. **Such transactions do happen, however, in the value-in-use net lease market.** Once again, the comparison shows that the value-in use net lease sale price is completely unrelated to the value of the underlying, fee simple real estate. In fact, the former Kmart property is actually located in a superior area by many measures, including area rents, occupancy, development activity, and household income. (Appellant's Supplement, p. 137; Lorms, p. 54). Yet the Lowe's property sold for almost twice as much. This is inexplicable on the basis of the unencumbered, fee simple value of the real estate. The vast divergence can only be explained by either (1) the credit-worthiness of Lowe's, or (2) the fact that, as discussed by Mr. Lorms on page 20 of his report (Appellant's Supplement, p. 103), a build-to suit lease, as is the case with the Lowe's lease, does not reflect any market obsolescence but rather, the value to them as the tenant. Neither of these two factors is present in the sale of the unencumbered former Kmart in a superior location.

The last example concerns the Walgreens at Demorest and Clime in Columbus. At the opposite corner to the Walgreens drugstore, there is a CVS drugstore. Below are the characteristics of each.

<p align="center">Sale Comparison 3 (At the same intersection two comparable drugstore properties sell for significantly different values)</p>					
Property	Year Built	Sale Date	GLA	Price Per SF	(Demographics) Population HH Income Housing Value
Walgreens 1280 Demorest Rd. Columbus, Ohio	2002	9/4/02	14,490	\$271.74	Same intersection
CVS (same corner) 3499 Clime Rd Columbus, Ohio	1999	7/26/04	10,113	\$206.90	Same intersection

(see *Board of Edn. of the Columbus City Schools v. Franklin Cty. Bd. of Revision* (May 18, 2007), BTA Case Nos. 2005-R-329 and 330, unreported, *on appeal to the Ohio Supreme Court* docket number 2007-1086.)

It seems difficult to explain how a similar drugstore at the same intersection would be worth 30% more than the other. Again, this sale reflects that **value-in-use net lease market transfer prices are not guided by real estate fundamentals**. Just over a 30% difference in value for nearly identical properties *at the same intersection* is once again inexplicable on the grounds of real estate considerations. In fact, the CVS property sold almost two years later, over which time property values presumably went up. Certainly, these sales cannot be considered to be the best evidence of real estate value for each property, as their divergent sale prices cannot reasonably be reconciled. The differences in the sale price can only be accounted for if we go beyond the underlying real estate and consider the differences in the success and credit-worthiness of Walgreen and CVS. Assessing the subject in accordance with its sale price, therefore, would be assessing Walgreens as a business, not the real estate. Such an assessment is prohibited by Ohio law. This transaction will also be revisited, *infra*, as it reflects almost

perfectly the hypothetical scenario outlined and rejected as evidence of value by this Court in *Higbee Co. v. Cuyahoga Cty. Bd. of Revision* (2006), 107 Ohio St. 3d 325.

**THE PRINCIPLE OF SUBSTITUTION PROVIDES FURTHER
EVIDENCE THAT THE SALE PRICE IS NOT CORRELATED TO THE
VALUE OF THE REAL ESTATE**

Another aspect of the instant matter that supports the proposition that the sale of the subject property is not reflective of its real estate value can be derived from the principle of substitution. According to the principle of substitution, “a prudent buyer would pay no more for a property than the cost to acquire a similar site and construct improvements of equivalent desirability and utility without undue delay.” (*The Appraisal of Real Estate*, 12th Ed. p. 350).

The brand new replacement cost estimate of the subject’s land and improvements determined by Mr. Lorms is \$11,572,843 (Appellant’s Supplement, pp. 142-145; Lorms, pp. 59-62), disregarding for the purpose of this argument the significant amount of depreciation identified by Mr. Lorms. Although, as discussed in detail below, the Property Owner disagrees with the county’s appraiser, Ms. Ebert, the conclusions here do not change if the higher land value determined by Ms. Ebert is utilized. Although Ms. Ebert did not utilize the cost approach to value the improvements if the replacement cost new determined by Mr. Lorms is added to Ms. Ebert’s land value, the replacement cost for a brand new building is \$13,473,843. (Appellant’s Supplement, p. 145 and 311; Lorms, p. 62; Ebert, p. 48). Even though the subject property at the time of sale is already eight years old the sale price for an eight year old building exceeds the cost to acquire the land and build a brand new building by either \$4,345,157 or \$2,444,157. As such, the purchase price is approximately 37.5% higher than the replacement cost new determined by Mr. Lorms, ignoring any depreciation. Even if the higher replacement cost new utilizing the land values determined by Ms. Ebert, which the Property Owner does not accept, is

utilized, the purchase price is still approximately 18% higher than the cost to purchase the land and build the exact same **new** building.

Whether utilizing Mr. Lorms well-supported replacement cost or the hypothetical, unsupported replacement cost utilizing Ms. Ebert's land values, both estimates are significantly below the purchase price of the subject property. Why would a buyer pay so much more for an eight-year-old property than it would cost to build **brand new**? Clearly, as both discussed by Mr. Lorms and demonstrated by significant market evidence in his report, a lease to a successful and credit-worthy tenant influenced the price paid for the subject property. The sale in this case is so at odds with the principle of substitution that either a well-established principle of appraisal theory is wrong, or the sale of the subject property is not correlated to the value of the real estate. As Mr. Lorms stated,

Well, that's one of the reasons that I frown on using net lease sales, especially for ad valorem taxes. Many times we'll see the sale and whether it's a Walgreens, a Wal-Mart, or in the subject's case or whatever, you will see a very high price when you look at a per square foot. And so that's the first red flag is to say that here's a sale of property that might be several hundreds of dollars per square foot and yet you know the cost to buy the site and replace the building is significantly less. And so you're saying there must be a difference then because if I can go out and buy a site and replicate those buildings for "X" dollars -- Well, let's just take a look at our appraisal for example. In our cost approach, we say we think land is worth \$4,200,000, and we estimate the replacement cost new rounded to about seven million four, that would cost about \$11,600,000 to buy that site and put this building up. And yet you see maybe a transfer or sale of that same property substantially greater than those costs, that alerts me that there is something going on in the transaction other than a real estate deal. There's something -- There's an intangible here that has to do with the going business concern and the creditworthiness of that tenant if someone is willing to pay such a premium for the replacement costs for a site. So that's one instance of why I take issue with some net lease sales especially with reference to a fee simple market value. (Appellant's Supplement, p. 40; Tr., pp. 151-152).

It is the Property Owner's position that it is the sale price that is unreliable, not the principle of substitution.

As discussed above, the sale of the subject property is reflective of its value in use to the user for which it was built. The property was built to suit for Wal-Mart. Given a floor plan tailored to Wal-Mart's unique requirements, the construction costs reflect a value in use to Wal-Mart. The resulting lease was designed to amortize these value-in-use construction costs. The property was subject to this lease at the time of its sale in the net lease market. The net lease market, as demonstrated by the examples above, is motivated by non-real estate factors. Considering all of the unique characteristics of both this property and the market in which it transferred, the sale of this property is not reflective of its unencumbered, fee simple value.

III. To adopt the sale price as the value of the subject property, it would be inconsistent with this Court's holding in *Higbee Co. v. Cuyahoga Cty. Bd. of Revision* (2006), 107 Ohio St. 3d 325, wherein this Court rejected evidence of value inextricably intertwined with the non-real estate business value of the tenant.¹⁰

In *Higbee*, the Taxpayer proffered evidence in which the valuation of a single-tenant retail property was based upon the gross sales of a tenant. This Court rejected this approach as an impermissible valuation of the property essentially in use. In rejecting a valuation based on gross sales, this Court held:

If it is the real property being valued, its valuation cannot be made to vary depending on the success or lack thereof of the businesses located on the property. Admittedly, the location of a property may influence the sales made by a merchant at that property. However, the merchant's business practices may also influence sales. The business factors and the real-property factors must be separated when the real property is being valued for tax purposes. *Higbee, supra*, at 395.

¹⁰ This Proposition of Law addresses Assignments of Error 1, 2, 3, 4, 5, 14, 15, 16, 20 and 23.

This Court acknowledged that gross sales could vary by location, but the influence of the business practices would remain with the tenant. That is, while gross sales could be partially attributable to the location of the real estate, they could also be attributable to the success or lack thereof of the tenant as a business, and therefore this Court rejected valuation based on gross sales. Similarly, in this case, the business practices of the tenant, Wal-Mart, have resulted in significantly above average credit-worthiness, which in turn drives the resulting sale price higher than it would otherwise be. Whether it is gross sales or credit-worthiness, both are a function of the tenant. In fact, credit-worthiness has an even stronger correlation with the tenant's business practices than gross sales does. Indeed, gross sales for the same tenant, say, Wal-Mart, can vary by location, but their credit-worthiness remains constant no matter which location they are operating from. As such, there would tend to be an even greater non-real estate component that is a function of credit-worthiness when compared to gross sales. If gross sales impermissibly clouded the value in *Higbee*, the successful business practices of Wal-Mart and its above-average credit-worthiness, which artificially inflated the sale price, should be of even greater concern to this Court.

The fact that the sale price in this case was driven by the success and credit-worthiness of Wal-Mart seems beyond dispute, as the appraisers for both the Property Owner and the County have agreed. (Appellant's Supplement, p. 87 and 312; Lorms, p. 4; Ebert, p. 49). Even the BTA, just weeks before it erroneously felt constrained by *Berea*, agreed with the position that the kind of sale at issue in the instant matter is a function of its use-value and the success and credit-worthiness of the tenant. In *Dayton*, when the BTA considered the valuation of a Rite Aid store, it concluded:

Nevertheless, [the BOE's appraiser's] opinion of value is borne from his exclusive reliance on the sixteen similar build-to-suit

comparables, all of which present the same issues concerning the occupants' credit-worthiness and the like. The data gleaned from the comparables appear to be tied (as is in the case of the subject) to the credit-worthiness of their tenants. The difficulty in relying upon income derived from a business activity, or **value in use**, is that the value ultimately derived may not be the market value of the subject property. *Dayton, supra*.

In the instant matter, even the County's own appraiser, Ms. Ebert, admitted that the sale price of the subject property and other net-leased properties are driven by the business success and credit-worthiness of the tenant. According to Ms. Ebert, "[t]hese types of sales are 'Credit Tenant Net Lease Properties.' They are called Credit Tenant Net Lease properties because the credit-worthiness of the tenant is a major component in determining sales price and desirability to investors." (Appellant's Supplement, p. 312; Ebert, p. 49).

On behalf of the Property Owner, Mr. Lorms further elaborates on this point in his appraisal:

The tenant's credit is significantly above average and the length of the lease is significantly longer than average, both of which decrease the applicable capitalization rate and increase the market value of the leased fee interest. The tenant's credit is reflective of the strength of the business operation conducted by the tenant. Therefore, the sale price is positively influenced by economic characteristics which are atypical of most properties. In addition, the buyer was not buying the "right to lease an interest or occupy property." Therefore, the rights purchased did not meet the definition of the fee simple estate or provide an equivalent value indication. Rather, they reflect the underlying value of the business using the property. When it is unencumbered real property that is being valued, its valuation should not be made to vary based upon the success or lack thereof of the business located on the property." (Appellant's Supplement, p. 87; Lorms, p. 4).

This Court further illuminated the problems associated with allowing a tenant's business success to influence the assessment of the real property, discussing the following scenario:

Assume two identical anchor department store buildings in the same mall, operated by different owners. If one store has higher

sales per square foot than the other, is the property housing the store with the lower sales worth less than the building housing the store with the higher sales? While the store with the higher sales per square foot may be worth more as a business, that consideration must be separated from a valuation of the real property. The two buildings in the hypothetical mall should be valued the same if they are identical. *Higbee* at p. 334.

Also consider the hypothetical described by Mr. Lorms in his appraisal:

As a final example of why these build-to-suit leased fee transfers can not be used as an indication of the market value of the fee simple estate, we provide a hypothetical situation where two identical retail buildings are sitting side by side, with identical physical characteristics and identical lease circumstances, except one is occupied by Wal-Mart and the other is occupied by Kmart. While the fundamental real estate characteristics are identical and the market value of the fee simple estate should be identical, the Wal-Mart store would have a significantly higher leased fee value because of the success of Wal-Mart's business operations and the resulting superior credit-worthiness and the lower applicable capitalization rate." (Appellant's Supplement, p. 139; Lorms, p. 56).

Such a difference in capitalization rates is confirmed by Ms. Ebert when she includes the average capitalization rates for Wal-Mart and Kmart in her report. A Kmart leased property would sell at a capitalization rate of 8.82% while the Wal-Mart store at 7.56%. (Appellant's Supplement, p. 324; Ebert, p. 61). Utilizing the hypothetical situation of two identical stores side-by-side to carry the effect of this difference into actual value, if each property had the same operating income from real estate determined by Mr. Lorms of \$467,167 (Appellant's Supplement, p. 166; Lorms, p. 83), the Wal-Mart property would sell for \$6,179,458 while the Kmart property would be expected to sell for \$5,296,678. A difference of \$882,780 or that the Wal-Mart property would sell for 16.67% higher than the Kmart property. The overwhelming market evidence provided by Mr. Lorms and even the limited market evidence supplied by Ms. Ebert in her

report supports the fact that this small subset of sales are not reflective of the fee simple, true value of these properties.

Additionally, as discussed above, the hypothetical examples that concerned both this Court in *Higbee* and Mr. Lorms in his appraisal have come to fruition in actual transactions in the market. Recall that the CVS and the Walgreens stores at Demorest sold for widely different prices, even though they are located at the same intersection and are essentially the same real estate. It is essentially the same situation as the hypothetical this Court discussed in *Higbee* and Mr. Lorms discussed in his appraisal. (*Higbee*, at 334; Appellant's Supplement, pp. 138-139; Lorms, pp. 55-56).

There appears to be substantial agreement between the parties in this case, their appraisers, the BTA in *Dayton* just prior to *Berea*, and this Court in *Higbee*. It is the opinions of Ms. Ebert for the County, Mr. Lorms for the Property Owner, and the pre-*Berea* BTA in *Dayton*, *supra*, that the sale of the subject property was a function of the success and credit-worthiness of the tenant and its value-in-use. Therefore, pursuant to this Court's holding in *Higbee*, the sale of the subject property must be rejected as the best evidence of value.

IV. It would be inconsistent with prior decisions of this Court, including most recently *Strongsville Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision* (2007), 112 Ohio St. 3d 309, that rejected similar sale and leaseback transactions to accept the sale price of the subject property.¹¹

This Court has consistently rejected as evidence of value a sale that involves a sale/leaseback transaction. See *Strongsville Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision* (2007), 112 Ohio St. 3d 309; *S. Euclid/Lyndhurst Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision* (1996), 74 Ohio St. 3d 314, 317; *Kroger Co. v. Hamilton Cty. Bd. of Revision* (1993), 67 Ohio

¹¹ This Proposition of Law addresses Assignments of Error 7, 8, 15 and 19.

St. 3d 145; *Cleveland Hts./Univ. Hts. Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision* (1995), 72 Ohio St. 3d 189; *Pingue v. Franklin Cty. Bd. of Revision* (1999), 87 Ohio St. 3d 62. In these cases, this Court concluded that such sales are nothing more than financing transactions for the underlying real estate. In the typical sale/leaseback transaction, the user builds the building, sells it, and leases it back. This type of transaction is virtually identical in both structure and purpose to the build-to-suit, net lease sale that is the basis of the school board's opinion of value in the instant matter. In both types of transactions, the leases are designed to amortize the costs of development, while allowing the user greater financial flexibility. As Mr. Lorms testified:

Whether the user designs, builds, and owns their own facility; designs, builds, and enters into a sale/leaseback transaction; or enters into a build to suit lease agreement with a developer, the development costs, sale price, or lease rates are driven by the value in use to the business enterprise. (Appellant's Supplement, p. 131; Lorms, p. 48).

Mr. Lorms elaborates further on this point:

Where a building is designed and constructed to meet the user's specific needs, regardless of whether the ultimate transaction results in the user leasing the new building, purchasing it from the developer, or building it itself and then selling to an investor (sale/leaseback), the final outcome is identical – a financial transaction to accommodate the value-in-use by the specific user. The value reflected by that transaction is unique to that specific user and not, in and of itself, reflective of the market value or value in exchange of the property.” (Appellant's Supplement, p. 132; Lorms, p. 49).

In its most recent decision concerning the utilization of sale/leaseback transaction, this Court in *Strongsville* reaffirms its rejection of sale/leaseback transactions as not reflective of fair market value. *Strongsville*, at 13. In the case of *Strongsville*, the rejection is based upon elements of duress. In so holding, however, this Court cites with approval *Kroger Co. v. Hamilton Cty. Bd. of Revision* (1993), 67 Ohio St. 3d 145, in which this Court rejected a

sale/leaseback transaction due to the absence of an open market. As discussed above, the entire process of building the subject property and entering into the lease is a closed transaction not open to the market. (Appellant's Supplement, p. 86; Lorms, p. 3). Indeed, the Appraisal of Real Estate and this Court have repeatedly emphasized the importance of exposure to the open market before properly relying on a transaction. (See, *Kroger, supra*).¹² This fact alone should render the instant sale suspect.

In *Strongsville*, this Court found that *Berea* did not end any and all inquiries into the reliability of a given sale. When the BTA received evidence sufficient to rebut the presumption that the *Strongsville* sale was not arm's length, this Court found the BTA correctly rejected the sale as the best evidence of value. However, in the instant matter, the BTA erroneously failed to make an equally important determination – whether the lease that encumbered the property at the time of the sale, which formed the basis for the purchase price, was itself an arm's length transaction.

As the original lease was not an arm's length transaction, it follows that any subsequent sale based upon that lease would render it unreliable. As Mr. Lorms states in his report,

The lease rate was negotiated prior to construction between Wal-Mart and the developer and the property was never available on the open market. In these build to suit arrangements, the developer acts as an outsourcing of the financing and construction for the retailer. The tenant selects the site and gives the developer all of the design and construction specifications. Wal-Mart has a specific rent-to-cost factor that determines the rent to be paid. Therefore, the rent is pre-determined, based on an amortization of the construction costs, and doesn't take what the property would lease for on the open market into consideration. (Appellant's Supplement, p. 86; Lorms, p. 3).

¹² According to the Appraisal of Real Estate, 12th Ed., p. 83, market rent is "[t]he rental income that a property would probably command in the *open market*." (Emphasis added). In its definition of market value, the Appraisal of Real Estate, 12th Ed. p. 22, indicates that it is "[t]he most probable price . . . for which the specified property rights should sell *after reasonable exposure in a competitive market*." (Emphasis added).

The lease is never negotiated on the open market. . . . In summary, the developer essentially acts as a financing and construction arm of the user/tenant and the characteristics of the arrangement do not meet the definition of an arm's length transaction." (Appellant's Supplement, p. 103; Lorms, p. 20).

It must be emphasized that the Property Owner's contention that the original lease does not meet the characteristics of an arm's length lease was never challenged by the Appellees or the BTA. In addition, there is no dispute that the purchase price for the property was driven by the lease. Consequently, any sale based upon a lease that is not arm's length must itself be rejected as an unreliable indication of value.

In *Strongsville*, the property owner negotiated a sale and leaseback arrangement, which the BTA, in this Court's view, properly rejected as the best evidence of value. Surely, if the sale and leaseback was not arm's length, any subsequent purchase based upon the same lease would be equally suspect. Similarly, in the instant matter, if the original lease was not arm's length, any subsequent sale cannot be relied upon. At minimum, the suspect nature of the original lease rebuts the presumption that the sale is the best evidence of value.

Because sale/leaseback transactions have been repeatedly rejected by this Court as indicators of value, and since value-in-use, net lease transactions have the same inherent unreliability in reflecting the unencumbered, fee simple value of the property, this Court should also reject value-in-use net lease sales which are similar in character to sale/leaseback transactions.

V. The testimony of the appraisers concerning the facts and circumstances surrounding the transfer of the property, and the characterization of the transfer's unreliability as an indication of value, constitutes admissible, competent, and probative evidence before the BTA.¹³

¹³ This Proposition of Law addresses Assignments of Error 9, 14, 16, 17, 18 and 21.

The BTA erred in not finding that the Property Owner had provided competent evidence concerning the facts surrounding the transfer in question. As has been discussed and demonstrated above, the appraisal and testimony of Mr. Lorms and well as the appraisal and testimony of the county's appraiser, Ms. Ebert, clearly demonstrates that the transfer in question is not reflective of the unencumbered fee simple value in exchange. The testimony of expert witnesses to provide such information is clearly contemplated and allowed by the Rules of Evidence. Preliminarily, Rule of Evidence 602 provides that

A witness may not testify to a matter unless evidence is introduced sufficient to support a finding that he has personal knowledge of the matter. Evidence to prove personal knowledge may, but need not, consist of the testimony of the witness himself. **This rule is subject to the provisions of Rule 703, relating to opinion testimony by expert witnesses.** (Evid. R. 602, emphasis added).

The reference in Rule 602 to Rule 703 is designed to avoid any question of conflict between the two rules, the latter of which permits an expert to express opinions based on facts of which the expert does not have personal knowledge. Specifically, Rule 703 provides that:

The facts or data in the particular case upon which an expert bases an opinion or inference may be those perceived by or made known to the expert at or before the hearing. **If of a type reasonably relied upon by experts in the particular field in forming opinions or inferences upon the subject, the facts or data need not be admissible in evidence in order for the opinion or inference to be admitted.** (Evid. R. 703, emphasis added).

There is no question that the reports and testimony of both appraisers is admissible as it relates to the transaction in question. First, the fact that information relied by Mr. Lorms and Ms. Ebert was clearly made known to both appraisers prior to the trials as not only was it a part of each appraiser's testimony but also included in the appraisal report of both appraisers. Secondly, it is beyond question that information regarding a facts and circumstances surrounding a sale is of the "type reasonably relied upon by [appraisers] in forming opinions or inferences."

This conclusion is further supported by the Notes to Rule 703. The Notes discuss the various sources of information which experts can rely in providing testimony. The type of information at issue in this case is covered under the third set of reliable information. These Notes date back to the 1972 and provide:

The third source contemplated by the rule consists of presentation of data to the expert outside of court and other than by his own perception. In this respect the rule is designed to broaden the basis for expert opinions beyond that current in many jurisdictions and to bring the judicial practice into line with the practice of the experts themselves when not in court. (1972 Notes to Evid. R. 703).

In *Worthington City Schools v. ABCO Insulation* (1992), 84 Ohio App.3d 144, 152, the court stated:

Some hearsay evidence necessarily is always involved with expert testimony. To become an expert, one must read and learn from sources which are necessarily outside the evidence at trial. It is this knowledge obtained from outside sources which qualifies a witness as an expert. (Citation omitted.) However, the facts or data which an expert relies upon in testifying must be either perceived by the expert or based upon evidence admitted at trial. Evid. R. 703.

The requirement of "perceived by the expert" refers to personal knowledge. Such perception and knowledge is recognized as being present in the case of an appraiser. *State v. Solomon* (1991), 59 Ohio St.3d 124, syllabus, held that "[w]here an expert bases his opinion, in whole or major part, on facts or data perceived by him, the requirement of Evid. R. 703 has been satisfied." In *Worthington City Schools v. ABCO Insulation* at 153, the court, in finding that the trial court did not abuse its discretion in admitting an expert's testimony, stated:

Here, the expert prepared the report personally, since he was the author. He had personal knowledge of the predicate for the contents of the article, so the facts were 'perceived by him' as required by Evid. R. 703.

Indeed, what is the job of an appraiser if it is not to determine whether a sale is arm's length, if it is indicative of value, or it reflects the use-value of the property? Appraisers by necessity speak with brokers, owners, and property managers to find out details about a sale or a lease. Based on their experience and education, they make judgments about such issues. These are the decisions appraisers make as a necessary part of including data in their appraisals. Some data passes their professional tests such that it can be relied upon and included in their appraisals, and some data fails to meet the proper standard. If the actual property owner in this case came to the BTA and declared that the sale is not reliable, or is a reflection of the value of the property in-use, the Appellees would have undoubtedly objected on the grounds that the owner does not possess the requisite knowledge or education to make such characterizations. This is not a situation where the expert was asked to testify in lieu of the buyer or the seller, but, rather, one that required the opinion of an expert to characterize the reliability of the transfer. The use-value issue, in particular, is a characterization that an appraiser seems uniquely qualified to support, pursuant to their education about such matters.

The testimony of both experts, Mr. Lorms and Ms. Ebert, provides competent evidence as to the facts and circumstances surrounding the transfer of the subject property, as well as the characterization of its reliability. Such testimony is clearly the intent of Rule of Evidence 703. It is without question that expert opinion of Mr. Lorms and Ms. Ebert in this case relates to facts that are of the type reasonably relied upon by appraisers in forming opinions or inferences.

VI. Adoption of the sale price in this case is inconsistent with Ohio law, succinctly stated by this Court in *Alliance Towers, Ltd. v. Stark Cty. Bd. of Revision* (1988), 37 Ohio St.3d 16, that it is the unencumbered fee simple value of the property which is to be valued for real property tax purposes.¹⁴

¹⁴ This Proposition of Law addresses Assignments of Error 5, 7, 12 and 19.

As discussed above, reliance upon the transfer price would violate a fundamental principle of Ohio's real property tax law - that it is the unencumbered, fee simple value of the property which is to be valued and taxed. That is exactly why in *Alliance Towers, Ltd. v. Stark Cty. Bd. of Revision* (1988), 37 Ohio St.3d 16, paragraph one of the syllabus, this Court held: "For real property tax purposes, the fee simple estate is to be valued as if it were unencumbered."

This Court further stated:

It is the fair market value of the property in its unrestricted form of title which is to be valued. It is to be valued free of the ownership of lesser estates such as leasehold interests, ***. For real property tax purposes, the fee simple estate is to be valued as if it were unencumbered. *Id.* at 23.

As discussed in *Alliance Towers*, for over 100 years, Ohio law has held that the unencumbered, fee simple interest in the property is to be valued. The properties in *Alliance Towers* are not unlike the instant property before this Court. In *Alliance Towers*, the apartment buildings were constructed at a cost greater than could be justified by market rents. Without government subsidies, this Court found, the developer would not have had sufficient rental income to justify the project. Here, as demonstrated in this case by Mr. Lorms, the feasibility rent needed to support the construction costs of the subject property significantly exceeds the market rent that could be achieved if the property were held out for lease on the open market. (Appellant's Supplement, pp. 146-147; Lorms, pp. 63-64). Furthermore, as Mr. Lorms discusses on page 3 of his report (Appellant's Supplement, p. 86), the lease rate was negotiated prior to the commencement of construction and is based upon construction costs that reflect the value of the property to the user, Wal-Mart, not the value of the property on the open market.

As this Court summarized in *Alliance Towers*:

These tax and eminent domain cases demonstrate the decision by this court to view the fair market value of real property as

uncomplicated by encumbrances. It is the fair market value of the property in its unrestricted form of title which is to be valued. It is to be valued free of the ownerships of lesser estates such as leasehold interests, deed restrictions, and restrictive contracts with the government. For real property tax purposes, the fee simple estate is to be valued as if it were unencumbered. *Alliance Towers* at p. 24.

If Ohio law were changed to allow for an assessment of the leasehold estate, overturning a century of assessment law in the process, the concerns raised by this Court in *Higbee*, further exemplified by real world transactions, (see the Brice Road/Mill Run big box sales and CVS/Walgreens Demorest sales discussed above), would come to fruition. Wal-Mart would pay more for the assessment of its stores than Kmart. Walgreens would pay more than Rite Aid. Best Buy would pay more than Circuit City. Staples would pay more than Office Depot. All for the same real estate. Such an assessment scheme cannot be allowed to engulf Ohio and further discourage business enterprise. Successful businesses already have their fair share of taxes that are a function of their success without having to pay higher real estate tax assessments too.

A lease that was never negotiated on the open market, for an amount significantly above what could be achieved on the open market, designed simply to amortize the costs of construction, and the subsequent sale of the subject property pursuant to that lease, has resulted in a sale price well in excess of the value of the fee simple estate. Accordingly, any assessment based upon that sale would result in an assessment of the leasehold estate which is far in excess of what this Court has long held to be the taxable, fee simple estate pursuant to *Alliance Towers*.

VII. Mr. Lorms' appraisal of the subject property constitutes competent, probative evidence of the value of the subject property.¹⁵

In his appraisal, Mr. Lorms relies on the cost, sales comparison, and income approaches to value. Preliminarily, recall that the area around the subject property has a declining

¹⁵ This Proposition of Law addresses Assignments of Error 7, 9, and 15.

population base and well below average income levels and housing values. (Appellant's Supplement, p. 101; Lorms, p. 18). In addition, the location of the subject property is well of the primary retail corridor and nowhere near any interchange, requiring Wal-Mart to erect a billboard directing customers to its remote location. (Appellant's Supplement, p. 36; Tr., pp. 134-136).

Turning to Mr. Lorms' cost approach, Mr. Lorms relies on six land sales between \$162,000/acre and \$416,000/acre to arrive at a fair market value of the subject's 14+ acres of \$4,200,000 or \$300,000 per acre. (Appellant's Supplement, p. 141; Lorms, p. 58). Unlike Ms. Ebert's minimal sales, including three sales below two acres, Mr. Lorms again relied on six sales, all of which were developed for other big box users in the greater Cincinnati area, with transaction dates before and after the tax lien date. (Appellant's Supplement, p. 141; Lorms, p. 58). Mr. Lorms then took a replacement cost estimate from Marshall's Valuation Service of \$7,373,843. (Appellant's Supplement, p. 145; Lorms, p. 62). After adding the value of the land, together with replacement cost of the building and site improvements, then deducting depreciation and obsolescence, Mr. Lorms arrived at a value of \$6,300,000 via the cost approach. (Appellant's Supplement, p. 151; Lorms, p. 68). Mr. Lorms' estimate of obsolescence was confirmed by three separate sources, including extraction from market sales, including supporting land values and depreciation estimates in the addendum; extraction from capitalized rent loss, and extraction from the sale and resale of three Kmart locations that sold subject to their original lease and then resold after they were closed. (Appellant's Supplement, pp. 146-150 and 216-223; Lorms, pp. 63-67, Lorms Addendum F for land sales and depreciation estimates).

In the sales comparison approach, Mr. Lorms relied on nine comparable sales ranging from \$34.92 per square foot to \$60.74 per square foot. (Appellant's Supplement, pp. 154-155;

Lorms, pp. 71-72). Summary information is provided in the appraisal report and complete write-ups on each sale are included in the Addendum E to the report. (Appellant's Supplement, pp. 196-205; Lorms, Addendum E). After consideration of various criteria, including location, size, age, and condition. Mr. Lorms reconciled to the middle of the range at \$45 per square foot, or \$6,000,000. (Appellant's Supplement, p. 157; Lorms, p. 74).

In his income approach, Mr. Lorms relied on ten market comparable rents ranging from \$1.25 per square foot to \$4.80 per square foot. (Appellant's Supplement, pp. 160-161; Lorms, pp. 77-78). One of the rents in close proximity to the subject was the former Winn Dixie on Glencrossing Way. (Appellant's Supplement, p. 160; Lorms, p. 77). It was leased to Steve and Barry's for a net effective rate of \$0 after accounting for rent concessions and build-out. (Appellant's Supplement, p. 160; Lorms, p. 77). This property is less than a mile away from the subject on the main retail corridor. Mr. Lorms concluded to a market rent at the upper end of the range at \$4 per square foot for the subject or a potential gross rent of \$595,700. (Appellant's Supplement, p. 163; Lorms, p. 80). Summary information is provided in the appraisal report and complete write-ups on each lease comparable are included in the Addendum E to the report. (Appellant's Supplement, pp. 206-215; Lorms, Addendum E). After adding expense reimbursements of \$336,900 and deducting 7% for vacancy and credit loss, Mr. Lorms arrived at an effective gross income of \$867,318. (Appellant's Supplement, p. 166; Lorms, p. 83). From his estimate of the gross income, Mr. Lorms deducted \$400,151 in expenses, including reserves, to arrive at a projected net income of \$467,167. (Appellant's Supplement, p. 166; Lorms, p. 83). Estimating a capitalization rate of 9.5% derived from three separate sources, Mr. Lorms concludes to a value of \$4,900,000 under the income approach. (Appellant's Supplement, p. 171; Lorms, p. 88).

Because of the significant amount of depreciation and obsolescence inherent in a built-to-suit drugstore, Mr. Lorms relied on his cost approach the least. (Appellant's Supplement, p. 172; Lorms, p. 89). Mr. Lorms gave primary consideration to the sales comparison approach which was further supported by the income approach in reconciling to a final value of \$6,000,000. (Appellant's Supplement, p. 172; Lorms, p. 89). This value was derived from 25 comparable indications, including six land sales, nine improved sales, and ten market rentals.

The School Board, before the BTA, strenuously raised two issues concerning Mr. Lorms' report that it claims undercuts his conclusion. The first argument is the classic red herring - if the store went dark, the location of the real estate must be bad. Mr. Lorms directly addresses this concern in his appraisal report. (Appellant's Supplement, pp. 152-153; Lorms, pp. 69-70). This argument by the School Board is the sort of knee jerk reaction that can also be rebutted upon brief, logical consideration. What the School Board fails to do is distinguish between a failed location and a failed tenant. Ames, Builder's Square, Big Bear, and Kmart are failed tenants who filed for bankruptcy. They presumably closed some stores in good locations and some stores in bad locations. No conclusion can be reached about a local, particular store because of the national bankruptcy of the user. For example, could a Wal-Mart succeed where a Kmart failed? Could a Target succeed where an Ames failed? Could a Lowe's succeed where a Builder's Square failed? The answer is self-evident and found in the market place across the state of Ohio.

Some perfect examples of the distinction between a failed tenant and a failed location can be seen in the comparables that Mr. Lorms utilized in his appraisal. Take the two Ames stores that were built for Ames but never occupied because they went bankrupt—comparables sales 3 and 5. (Appellant's Supplement, p. 154; Lorms, p. 71). The stores were purchased by Target

and Home Depot. Those locations have strong demographics and are surrounded by other users at the same location, including Wal-Mart, Kroger's, and Lowe's. Would Target and Home Depot purchase bad locations? Take the former Kmart purchased by Liberty Ford—comparable sale 4. (Appellant's Supplement, p. 154; Lorms, p. 71). Would a bad location be purchased by a new car dealership, which is itself across the street from Home Depot and Giant Eagle? Consider the Kmart at Mill Run—comparables sale 2. (Appellant's Supplement, p. 154; Lorms, p. 71). The surrounding users who are either succeeding or entering the market at the same location where Kmart failed are Lowe's, Target, Kroger's (former Big Bear), Home Depot and Staples. The Kmart on Ridge—comparable sale 6—is nearby a Wal-Mart and a Lowe's. (Appellant's Supplement, p. 155; Lorms, p. 72). The Builder's Square on Whipple Avenue—comparable sale 7—is near a regional shopping mall and numerous free-standing retail buildings. (Appellant's Supplement, p. 155; Lorms, p. 72). The examples are endless of users who failed where others succeed. So the mere fact that a user filed for bankruptcy says nothing about any particular location they may have vacated.

The School Board also argued that by focusing on sales of vacant buildings, Mr. Lorms is disregarding the economic characteristics of his comparable sales. Again, upon examination, the logic of the School Board is flawed. The key consideration is not the current cash flow being generated by a property, but the current economic capacity of the space. For example, say a buyer was looking at two retail stores to invest in. One was receiving \$1 per foot on a month to month lease. The other was vacant due to the bankruptcy of the former tenant, but the current owner was listing it for lease at \$6 per foot. All else being equal, would the store generating \$1 per foot on a month to month basis have a higher or lower fee simple value than the store that, although vacant, had an economic capacity to produce \$6 per square foot in rent? Additionally,

how about the former Ames stores purchased by Target and Home Depot? At the time of their purchase, those stores were empty. Would the fee simple value of those stores have been greater or less to Target or Home Depot if Ames occupied the space on a long term lease? Of course, Target and Home Depot, as users, wanted an empty building which had economic value to them, as evidenced by their purchase prices. Again, the School Board fails to distinguish between the actual cash flow of a property and its capacity for generating income.

Based upon the foregoing, the Property Owner would submit that the value of the subject property as determined by Mr. Lorms is well-supported and clearly inconsistent with its sale price, which reflected its use value, rather than the constitutionally mandated value-in-exchange.

VIII. The Auditor's appraisal by Ms. Ebert does not constitute competent, probative evidence of the value of the subject property.¹⁶

In addition to the sale of the subject property, the Auditor relied on the appraisal of Ms. Antoinette Ebert. Unlike Mr. Lorms, who is designated as an MAI and has decades of experience as an appraiser, Ms. Ebert has only been a state certified general real estate appraiser for four years. (Appellant's Supplement, p. 9; Tr., p. 25). She carries no designations, including MAI and, perhaps most importantly, she works exclusively for the Hamilton County Auditor. (Appellant's Supplement, p. 16; Tr., p. 53). What is most damaging to her credibility, however, is the materially false claim she makes in her disclosure statement. (Appellant's Supplement, p. 267; Ebert, p. 4). Specifically, even though Ms. Ebert is employed by the Hamilton County Auditor's office, and only does appraisals for the Auditor, she signed a document claiming that she was an unbiased and disinterested third party. Again, as an employee of the Auditor, who can only do appraisers for the Auditor, and who in this case has come up with a value highly

¹⁶ This Proposition of Law addresses Assignments of Error 7 and 9.

favorable to the Auditor's office, her claim of impartiality is particularly suspect. Ms. Ebert's verifiably false claim of impartiality should render her testimony and appraisal irrelevant and not credible.

Disregarding her false claim of impartiality, and turning to the merits of her appraisal, her entire appraisal suffers from the same fatal flaw that the sale of the subject property suffers as a reliable indication of value. Because almost all of her comparable sales and leases relate to build-to-suit, value-in use transactions, she is unable to make any sort of market based determination of value for the subject property.

The strained steps Ms. Ebert undertakes to support her valuation and then the inability to demonstrate a knowledge concerning the transactions relied upon undermines any attempt to rely upon the conclusions reached. Each of the valuation steps undertaken by Ms. Ebert will be reviewed.

The first thing Ms. Ebert does is arrive at a land value of over \$6,000,000. (Appellant's Supplement, p. 311; Ebert, p. 48). The basis for this land value is five sales, of which three are two acres or less, compared to the subject's 14 acres. (Appellant's Supplement, pp. 306-311; Ebert, pp. 43-48). If sales that are the equivalent of out-lots are ignored, as they should be, Ms. Ebert is left with two sales, one of which sold four years prior to the tax lien date. (Appellant's Supplement, p. 310; Ebert, p. 47). Thus, Ms. Ebert is left with one sale for \$8.24 per square foot of land, which would equate to a value for the subject land of just over \$5,000,000. This land sale on Harrison, however, is by Ms. Ebert's own admission in a superior location, with significant recent retail activity and direct access to an interchange. (Appellant's Supplement, pp. 20-21; Tr., pp. 72-75). The subject property has had no recent retail activity nearby, is nowhere near an interchange, and is even setback off an artery that is removed from its

main retail corridor. (Appellant's Supplement, p. 36; Tr., pp. 134-136).¹⁷ Accordingly, based upon one sale Ms. Ebert acknowledged was superior, there is either insufficient data in Ms. Ebert's report to come to a conclusion of value for the land or, alternatively, the indicated value is far below that which Ms. Ebert claims.

After attempting to value the land, Ms. Ebert turns to her sales comparison approach. She utilizes five comparable sales, not counting her listing of the subject property itself. The sales range from \$35.22 per square foot to \$221.49 per square foot. (Appellant's Supplement, p. 314; Ebert, p. 51). Two of her sales, the Kmart on Ridge Road and the Dillards in Western Hills support the value claimed by the Taxpayer. Of the remaining three sales, the Springdale sale is multi-tenant. (Appellant's Supplement, p. 318; Ebert, p. 55). As the Court is aware, the subject property is single tenant and, all else being equal, unable to command the same rents as smaller space in a multi-tenant building. Reliance on the sale of a multi-tenant building is misplaced. This leaves Ms. Ebert with two sales - a Circuit City in Cincinnati totaling 33,862 square feet and an HH Gregg in Cincinnati totaling 48,820 square feet. First, these are sales of properties that were built-to-suit for the users. (Appellant's Supplement, p. 24 and 25; Tr., p. 88 and 91). The sales, by Ms. Ebert's own admission as discussed above, are driven by the credit-worthiness of the tenants. For the same reasons the sale of the subject property represent its value in use, these also do not reflect the value of the underlying real estate that transferred. Even if they did, however, these stores are too small in comparison to the subject to be probative at all. Furthermore, going back to Ms. Ebert's questionable credibility, the HH Greg sale actually sold three times and Ms. Ebert decided to cherry pick the highest sale, even though there was a lower sale closer to the tax lien date. (Appellant's Supplement, p. 26; Tr., pp. 93-95).

¹⁷Although land sale five is four years old and, the Taxpayer would submit, irrelevant, Ms. Ebert also admits that this land sale is in a superior location, with recent retail activity and proximity to an interchange.

Finally, in Ms. Ebert's income approach she seems to rely on four leases and a sublease to arrive at an indicated market rent for the subject. (Appellant's Supplement, p. 322; Ebert, p. 59). However, one of those indications is the subject itself, which is disqualifying if the objective is to determine the market rent of the subject based upon comparables from the market. This leaves Ms. Ebert with three rent comparables and a sublease. None of the leases originated within two years or even eight years prior to the tax lien date. (Appellant's Supplement, pp. 28-29; Tr., pp. 101-106). These comparables are too remote to provide any indication of the appropriate rent for the subject as of January 1, 2004. Eliminating these old "comparables" leaves Ms. Ebert with a single rent comparable that is at all proximate to the lien date - the \$2.79 per square foot lease of a former Sam's Club. Yet even though this is her only rent comparable anywhere near the tax lien date, Ms. Ebert reconciles to a market rent for the subject of \$7.95 per square foot. (Appellant's Supplement, p. 322; Ebert, p. 59). This is not even remotely supported by her evidence.

After manufacturing her market rent for the subject, Ms. Ebert projects an income and capitalizes it by 7.6%. Interestingly, Ms. Ebert's capitalization rate is nearly identical to the surveyed rate for other Wal-Mart properties nationwide. (Appellant's Supplement, p. 324; Ebert, p. 61). She admits that the Wal-Mart capitalization rate is far less than the capitalization rate for other users such as Kmart. (Appellant's Supplement, p. 324; Ebert, p. 61). Again, as discussed at length, this just confirms that Ms. Ebert, in order to justify a value consistent with the sale price, felt compelled to value the subject in use, including a capitalization rate that can only be justified by having a tenant such as Wal-Mart as the occupant.

Ms. Ebert presents two approaches to value—the sales comparison and the income approach. Based upon the above analysis of the flaws contained in each approach, the Auditor

has failed to present any competent, probative evidence to establish the value of the subject property.

CONCLUSION

The sale of the subject property is not indicative of the market value of the real estate, but the value-in-use of the subject to a highly successful tenant. This conclusion is supported by the record in this case, appraisal theory, and overwhelming confirmation from sales that occurred in the market under similar circumstances. If there were any correlation between value-in-use, net lease sale prices and the value of the underlying real estate, the Kenny Road Walgreens would not have sold for less than the South High Street property. Similarly, the Brice Road Lowe's would not have sold for nearly twice as much as a practically identical property on Mill Run, a better location. And the Demorest Walgreens would not sell for 30% more than a CVS at the same intersection. These transactions demonstrate that the sale prices of properties such as the subject are entirely unrelated to the value of the underlying real estate.

Further proof of this can be found in the fact that the sale of the subject was well in excess of its replacement cost, contradicting the well-established principle of substitution that no buyer would pay more for a property than it would cost to build a similar property. In this case, however, the purchase price for an eight-year-old building was over 37.5% higher than the cost to replace the property **with a new building**. No buyer would do that unless the transfer price reflects the value of the Wal-Mart lease.

The sale is also functionally equivalent to other types of evidence of value rejected by this Court, including evidence of valuations intertwined with the success of the tenant as a business as seen in *Higbee*. In the instant case, the sale price is undeniably linked to the successful business practices of Wal-Mart and its above-average credit-worthiness. Therefore,

acceptance of the sale price in the instant matter would be contrary to this Court's mandate in *Higbee*. Finally, the *Berea* case is not relevant to the instant matter as the *Berea* sale did not reflect the value of that property in use or the success and credit-worthiness of the tenants.

The Property Owner has further offered competent, probative appraisal evidence in support of an unencumbered, fee simple value of the subject property. The appraisal report presented on behalf of the Auditor is seriously flawed and not indicative of the unencumbered, fee simple market value of the subject property.

For all of the foregoing reasons, the Property Owner respectfully submits that the decision of the BTA is unreasonable and unlawful. Accordingly, the Property Owner respectfully requests that this Court reverse that decision and find that the value of the subject property as of the tax lien date was \$6,000,000. Alternatively, due to the failure of the BTA to properly consider the testimony of the expert witnesses, the Property Owner would respectfully request that this matter be remanded to the BTA with instructions that the sale is not reflective of the value of the subject property and the BTA should analyze the reports and testimony of the experts to arrive at the value of the subject property.

Respectfully submitted,



Fred Siegel (0005855)

Jay P. Siegel (0067701)

Nicholas M.J. Ray (0068664) (Counsel of Record)

Siegel Siegel Johnson & Jennings Co

3001 Bethel Rd., Suite 208

Columbus, OH 43220

(614) 442-8885

Attorneys for Appellants

CERTIFICATE OF SERVICE

This is to certify that on this 6th day of September 2007, a copy of the Appellant Anchor Lyons Limited Partnership Brief and Appendix to the Appellant's Merit Brief was sent via regular U.S. mail to Thomas J. Scheve, Assistant Prosecuting Attorney, 230 East Ninth Street, Suite 4000, Cincinnati, OH 45202, David C. DiMuzio, David C. DiMuzio, Inc., 1900 Kroger Building, 1014 Vine Street, Cincinnati, Ohio, 45202, and Lawrence Pratt, Section Chief-Taxation, Marc Dann, Ohio Attorney General, 30 East Broad Street, 17th Floor, Columbus, OH 43215-3428.



Nicholas M.J. Ray, Esq.

8401-2004