Safeway, Inc.
Assessment Appeals Narrative

Summary

Safeway, Inc. is one of the largest food and drug retailers in North America, operating over 2,200 stores in the United States.

Safeway operates stores ranging in size from approximately 5,900 square feet to over 90,000 square feet. The size of a store is determined based on a number of considerations, including the needs of the community the store serves, the location and site plan, and the estimated return on capital invested. Safeway's primary new store prototype is 55,000 square feet, and is designed to accommodate changing consumer needs and achieve operating efficiencies. Most stores offer a wide selection of food and general merchandise, and feature a variety of specialty departments such as bakery, delicatessen, floral, and pharmacy.

The Assessor's Office has valued Safeway's store equipment, fixtures, and décor using the cost approach to value, but the Applicant has used the comparative sales approach to value. The Applicant believes that the percent good factors used by the Assessor's Office to value the aforementioned equipment do not provide an accurate estimate of fair market value. During this presentation, the Applicant will prove that his value approach produces the best estimate of fair market value.

Burden of Proof

Property Tax Rule 321 states:

> "Subject to exceptions set by law, it is presumed that the assessor has properly performed his or her duties. The effect of this presumption is to impose upon the applicant the burden of proving that the value on the assessment roll is not correct, or, where applicable, the property in question has not been otherwise correctly assessed. The law requires that the applicant present independent evidence relevant to the full value of the property or other issue presented by the application.
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> "If the applicant has presented evidence, and the assessor has also presented evidence, then the board must weigh all of the evidence to determine whether it has been established by a preponderance of the evidence that the assessor's determination is incorrect. The presumption that the assessor has properly performed his or her duties is not evidence and shall not be considered by the board in its deliberations."

The Value Concept

When it comes to defining "value" for property tax purposes, Rule 2 states that:

> "…the words 'full value', 'full cash value', 'cash value', 'actual value', and 'fair market value' mean the price at which a property, if exposed for sale in the open market with a reasonable time for the seller to find a purchaser, would transfer for cash or its equivalent under prevailing market conditions between parties who have knowledge of the uses to which the property may be put, both seeking to maximize their gains and neither being in a position to take advantage of the exigencies of the other."

Rule 3 provides several methods for calculating fair market value, but for this case, the comparative sales approach and the cost approach will be the focus.

Rule 4 provides instructions on how to apply the comparative sales approach to value. First, an appraiser must:

> "Convert a noncash sale price to its cash equivalent by estimating the value in cash of any tangible or intangible property other than cash which the seller accepted in full or partial payment for the subject property and adding it to the cash portion of the sale price and by deducting from the nominal sale price any amount which the seller paid in lieu of interest to a lender who supplied the grantee with part or all of the purchase money."

Next, the appraiser must:

> "Make such allowances as he deems appropriate for differences between a comparable property at the time of sale and the subject property on the valuation date, in physical attributes of the properties, location of the properties, legally enforceable restrictions on the properties' use, and the income and amenities which the properties are expected to produce."

Rule 6 outlines the steps to take when estimating fair market value through the cost approach. This is the default method used by the Assessor's Office when valuing business personal property, and it is also the method that has been used by the Applicant for the case being heard today. The Rule states that the cost approach:

> "…is used in conjunction with other value approaches and is preferred when neither reliable sales data (including sales of fractional interests) nor reliable income data are available and when the income from the property is not so regulated as to make such cost irrelevant. It is particularly appropriate for construction work in progress and for other property that has experienced relatively little physical deterioration, is not misplaced, is neither over- nor underimproved, and is not affected by other forms of depreciation or obsolescence."

Additionally, Rule 6 states that:

> "Reproduction or replacement cost shall be reduced by the amount that such cost is estimated to exceed the current value of the reproducible property by reason of physical deterioration, misplacement, over- or underimprovement, and other forms of depreciation or obsolescence. The percentage that the remainder represents of the reproduction or replacement cost is the property's percent good."

SBE and CAA

Prior to the guidelines developed by the California Assessors' Association (CAA), the State Board of Equalization (SBE) had its own internal guidelines, referred to as Policy 10. These guidelines were provided to county assessors to use in the absence of information sufficient enough to develop local estimates of economic lives. However, these guidelines were not based on any studies or analysis, but on the opinions and experience of SBE and county staff members.

Policy 10 was withdrawn in 1996, which led to the creation of the CAA-recommended guidelines. SBE staff has not been involved in the development of these recommended guidelines, and only a portion of the guidelines are the result of an in-depth lifing study. Furthermore, these guidelines are only meant to be a starting point in the determination of fair market value, as it is impossible for SBE staff to do an in-depth lifing study for every equipment category.

In October 2008, SBE considered adopting economic life guidelines to be included in Assessors' Handbook 581 (AH 581) consistent with CAA methodology. Two months later, after receiving input from interested parties, SBE decided not to adopt these guidelines. As of today, SBE has made no recommendation pertaining to the economic or average service life of grocery store equipment, so the county assessors typically follow the CAA recommended guideline.

Cost Approach

Every year, taxpayers are required to submit their 571-L Business Property Statement (BPS) to the Assessor's Office for valuation under the cost approach. The BPS provides the Assessor's Office with the information necessary to apply percent good factors to the taxpayer's acquisition costs, which results in a taxable value as of the lien date. All taxable business personal property is categorized by equipment type, and is further broken down by acquisition year, with a total acquisition cost listed for each year.

The Assessor's Office has applied percent good factors in accordance with the guidelines recommended by the CAA, which state that grocery store equipment should be valued using a 12-year average service life. It is the Applicant's opinion that these factors do not account for the rapid depreciation of this equipment due to all forms of extraordinary obsolescence. Furthermore, the Assessor's valuation is significantly inconsistent with the replacement cost published by Marshall & Swift. Based on the Applicant's research, using equipment sales gives a more reliable indicator of fair market value.

External and Functional Obsolescence

Supermarket technology is advancing at an exponential rate. Checkout stands are being replaced by technology that tracks a shopper's purchases by cameras and sends the bill later. Many consumers are no longer buying groceries in person, as they have opted to buy online. Government regulations are constantly changing the efficiency standards of commercial refrigeration, which has led to increased competition among equipment manufacturers. Each of these factors has caused some form of obsolescence in the type of equipment used in Safeway stores.

Due to changing industry standards and consumer taste, the average footprint for grocery stores has been gradually shrinking. With less equipment needed to furnish a store, a surplus of used equipment has been created, leading to decreased values.

In recent years, there has been a large influx of inexpensive equipment being imported from Asia. The equipment is not equal in quality to the traditional American-manufactured equipment used by Safeway, but many companies are opting to buy the new imports rather than the used domestic equipment. In order to stay competitive, used equipment values have had to decrease drastically.

Sales Information

When a Vons or Safeway store closes down, the equipment of that store is offered for sale to the public. The method used to sell this equipment is by auction, which is typical for this industry. Because it is normal practice to sell this equipment by auction, it is the Applicant's opinion that the sale prices are a good indicator of fair market value. The sales documents provided show that every other major company in the industry sells equipment in the same manner.

For as long as the company has been selling its equipment, the trends have not improved. An entire store typically sells for less than ten percent of the county's roll value.

The sales information submitted by the Applicant provide an excellent indicator that this equipment does not hold the value consistent with the way it is being treated by the Assessor's Office. Based on a variety of external factors, this equipment does a very poor job of maintaining its value.

Equipment sales have been analyzed on a price per square foot basis, with adjustments made for such things as equipment age, sales tax, and installation. The following are the locations that were considered for purposes of this analysis:

Name	**Location**	**Sale Date**	**Age**	**$/SF**
Haggen Food & Pharmacy	Los Angeles, CA	1/7/2016	10 years	$6.08/SF
Vons	Simi Valley, CA	1/26/2016	12 years	$4.71/SF
Walmart	Hawaiian Gardens, CA	5/11/2016	5 years	$9.72/SF

Name	Location	Sale Date	Age	$/SF
Walmart	Los Angeles, CA	6/1/2016	5 years	$6.74/SF
Ralphs	Oceanside, CA	8/4/2016	10 years	$3.76/SF
The Fresh Market	Shaker Heights, OH	9/15/2016	10 years	$6.49/SF
Fresh & Easy	San Diego, CA	1/4/2017	7 years	$5.84/SF
Kroger Supermarket	Louisville, KY	1/28/2017	12 years	$4.39/SF
Whole Foods	Prescott, AZ	3/16/2017	8 years	$6.29/SF
Fresh & Easy	Moreno Valley, CA	3/28/2017	10 years	$7.03/SF
Whole Foods	Encinitas, CA	6/8/2017	6 years	$8.03/SF
Whole Foods	Davis, CA	3/15/2018	6 years	$14.73/SF
Whole Foods	Overland Park, KS	6/5/2018	8 years	$5.49/SF
Whole Foods	Littleton, CO	11/29/2018	5 years	$7.93/SF
Fresh & Easy	Clovis, CA	12/13/2018	10 years	$6.33/SF

Marshall & Swift also recommends a price per square foot when estimating replacement cost, which has been matched up against the Applicant's comparative sales approach. While the replacement cost tends to be slightly higher than the comparative sales approach, both approaches yield results that are substantially lower than the Assessor's roll values.

Opinions from Industry Participants

Over the years, the Applicant has spoken with members of the grocery store industry who deal with equipment acquisition, disposal, and maintenance on a regular basis. Throughout a 25 year span, the message of these experts has remained the same; this equipment does not maintain the value indicated by using the 12-year average service life percent good factors.

The 12-year percent good factors do not account for installation costs that cannot be recovered when the equipment is sold by the original owner, especially in the first couple years of use. The factors do not account for excess physical obsolescence due to high foot traffic and misuse by customers. The factors do not account for functional obsolescence created by rapid advances in technology, especially in refrigeration. The factors also do not account for external obsolescence created by government regulations, also pertaining to refrigeration. All of these factors lead to early retirement for this type of equipment, usually at around eight to ten years of age.

Conclusion

In contrast to the Applicant's market research, the Assessor's Office has relied on the CAA recommended SBE 12-year average service life for grocery store equipment. Neither CAA nor SBE has provided documentation for the recommendation to use a 12-year average service life for this category of equipment. To the best of the Applicant's knowledge, neither group has performed an economic life study to support using a 12-year table.

In 1996, SBE released its Letter to Assessors (LTA) discussing the guidelines for the economic lives assigned to each equipment category per Policy 10. The LTA states that the economic lives are "based on the knowledge and experience of ASD's auditor appraisers, opinions of assessors and their staffs, and information from various industry sources. In most cases they were not based on actual studies of the average service lives of any of the listed groups of equipment." The LTA also states that the guidelines are "not to be cited as an authority in assessment appeals hearings. An assessment appeals case should be decided by applying the appropriate property tax statutes, regulations, court rulings, and sound appraisal practice to the pertinent information available for the situation in dispute."

When Policy 10 was replaced by CAA guidelines, the methodology used to determine average service life did not change. Just like before, the new guidelines were based primarily on opinions and experience, with little to no actual market research.

What this case comes down to is fair market value. There is a basic idea of how long the equipment can physically last, and how long the equipment stays in service on average, but the true goal is to find the equipment value after each year of use. Based on the market data, it is the Applicant's opinion that using a 12-year average service life to value this type of equipment is too conservative.

Property Tax Rule 324 states:

> "The board is not required to choose between the opinions of value promoted by the parties to the appeal, but shall make its own determination of value based upon the evidence properly admitted at the hearing."

And again, Property Tax Rule 321 states:

> "Subject to exceptions set by law, it is presumed that the assessor has properly performed his or her duties. The effect of this presumption is to impose upon the applicant the burden of proving that the value on the assessment roll is not correct, or, where applicable, the property in question has not been otherwise correctly assessed. The law requires that the applicant present independent evidence relevant to the full value of the property or other issue presented by the application.
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> "If the applicant has presented evidence, and the assessor has also presented evidence, then the board must weigh all of the evidence to determine whether it has been established by a preponderance of the evidence that the assessor's determination is incorrect. The presumption that the assessor has properly performed his or her duties is not evidence and shall not be considered by the board in its deliberations."

The Assessor's representatives have presented no evidence to support using a 12-year average service life besides the recommended guidelines instructing them to do so. The aforementioned LTA states that these recommended tables should not be cited as an authority in determining fair market value. There have been no studies, nor any market information presented to support valuing this equipment with 12-year trend factors. Therefore, the Applicant requests that the board enroll the following values for the January 1, 2018 lien date:

Address	**City**	**Acct No**	**Appeal No**	**Fixtures**	**Personal Property**	**Opinion of Value**
845 S Main St	Willits	079-0004376-002	18-026	0	382,311	382,311
660 S Main St	Fort Bragg	079-0004376-000	18-024	0	535,937	535,937
623 S State St	Ukiah	079-0004376-004	18-025	0	609,474	609,474
				0	**1,527,721**	**1,527,721**

We also request that the board enrolls the following values for the January 1, 2019 lien date:

Address	**City**	**Acct No**	**Appeal No**	**Fixtures**	**Personal Property**	**Opinion of Value**
845 S Main St	Willits	079-0004376-002	19-018	0	382,311	382,311
660 S Main St	Fort Bragg	079-0004376-000	19-016	0	535,937	535,937
623 S State St	Ukiah	079-0004376-004	19-017	0	609,474	609,474
				0	**1,527,721**	**1,527,721**