COURT OF APPEALS
DECISION
DATED AND FILED

December 28, 2016

Diane M. Fremgen
Clerk of Court of Appeals

Appeal No. 2015AP876 **Cir. Ct. No. 2012CV975**

STATE OF WISCONSIN **IN COURT OF APPEALS**
DISTRICT III

CVS PHARMACY, INC.,

PLAINTIFF-RESPONDENT,

V.

CITY OF APPLETON,

DEFENDANT-APPELLANT.

APPEAL from a judgment of the circuit court for Outagamie County: JOHN A. DES JARDINS, Judge. *Affirmed*.

Before Stark, P.J., Hruz and Seidl, JJ.

¶1 PER CURIAM. We are once again asked to review property tax assessments involving a national drugstore chain—this time CVS Pharmacy, Inc. The circuit court concluded that the City of Appleton's assessments were not entitled to a presumption of correctness because the assessments violated the

principles set forth in ***Walgreen Co. v. City of Madison*** (***Walgreen/Madison***), 2008 WI 80, 311 Wis. 2d 158, 752 N.W.2d 687, and CVS Pharmacy presented significant contrary evidence rebutting the City's assessments. Applying the holding in ***Walgreen/Madison***, we affirm the circuit court's decision.

BACKGROUND

¶2 CVS Pharmacy operates a one-story, single-tenant retail facility in the City of Appleton. CVS Pharmacy purchased the land for its facility in 2008 for $1,975,000. After acquiring the land, CVS Pharmacy tore down the existing building and hired a contractor to do site work and build a new retail store. The total cost to construct the new retail store amounted to $1,822,000.

¶3 After constructing the new store, CVS Pharmacy sold the property in 2009 to a real estate investment group for $4,459,470. The property was sold as part of a bundle of 166 CVS Pharmacy stores in a sale-leaseback transaction.[1] The long-term lease requires CVS Pharmacy to pay all taxes and maintenance costs associated with the property. In addition, CVS Pharmacy's rental payments under the lease are "tied to the repayment schedule" equal to the property's mortgage

[1] "A real estate sale-leaseback transaction is a transaction where the seller sells a real estate asset to a buyer, and then the buyer leases it back to the seller long term." Seth Chertok, *The Rise of the Dodd-Frank Act: How Dodd-Frank Will Likely Impact Private Equity Real Estate*, 16 U. PA. J. BUS. L. 97, 153 (2013).

payments. CVS Pharmacy's parent corporation, CVS Caremark,[2] guaranteed compliance with all of CVS Pharmacy's obligations under the lease.

¶4 The City assessed the property at $4,459,500 for 2011, 2012, and 2013, based on the 2009 purchase price. As a result, CVS Pharmacy commenced this action under WIS. STAT. § 74.37(3)(d) (2013-14),[3] alleging that the City's assessments in those years were excessive.

¶5 After considering the evidence at trial, the circuit court concluded that the City's tax assessments were not entitled to a presumption of correctness and were, in fact, excessive. First, the court determined that the City's reliance on the 2009 sale in determining the fair market value of the property was improper because "the subsequent leaseback [agreement] influenced the purchase price" above fair market value. Second, it determined that the City's reliance on recent sales of other properties—mostly Walgreens pharmacies—was improper because those properties' long-term leases caused the properties' sale prices to exceed their fair market value. Third, the court determined that the City's reliance on CVS Pharmacy's contract rents when utilizing the income approach was improper because those rents were above market given the underlying sale-leaseback transaction. Finally, the court determined that the City's reliance on the property's

[2] CVS Caremark changed its corporate name to "CVS Health" in 2014. *See* Jack Newsham, *CVS Caremark Changes Its Name to CVS Health*, BOS. GLOBE (Sept. 4, 2014), https://www.bostonglobe.com/business/2014/09/03/cvs-caremark-changes-its-name-cvs-health/bMCJa2fVQiBJ9rEX7szbXJ/story.html. However, we refer to the entity as CVS Caremark because that is what it was known as when it guaranteed CVS Pharmacy's obligations under the lease.

[3] All references to the Wisconsin Statutes are to the 2013-14 version unless otherwise noted.

2008 purchase price to value the land when utilizing the cost approach was improper because CVS Pharmacy presented significant contrary evidence.

¶6 Utilizing the cost, income, and comparable sales approaches, CVS Pharmacy experts opined that the property was worth between $1,500,000 and $2,000,000 on the assessment dates—much less than the City's $4,459,500 property assessment. Based on the testimony of CVS Pharmacy's experts, the circuit court concluded that the property's value was $1,690,000 in 2011; $1,760,000 in 2012; and $1,855,000 in 2013. The City now appeals.

DISCUSSION

¶7 This case involves an excessive tax assessment claim under WIS. STAT. § 74.37(3)(d). "This is not a certiorari review." ***Bloomer Housing Ltd. P'ship v. City of Bloomer***, 2002 WI App 252, ¶11, 257 Wis. 2d 883, 653 N.W.2d 309. Thus, "we [only] review the circuit court record." ***Walgreen/Madison***, 311 Wis. 2d 158, ¶16. The circuit court's factual findings will not be disturbed on appeal unless they are clearly erroneous. *See* WIS. STAT. § 805.17(2). As fact-finder, the circuit court determines the credibility and weight of expert witness testimony. *See* ***Bloomer Housing***, 257 Wis. 2d 883, ¶12.

¶8 Under WIS. STAT. § 70.32(1), assessors must value real property in accordance with the WISCONSIN PROPERTY ASSESSMENT MANUAL (2013) (hereinafter *Manual*),[4] unless the *Manual* conflicts with applicable law. ***Walgreen/Madison***, 311 Wis. 2d 158, ¶3. Assessments are entitled to a

[4] All references to the WISCONSIN PROPERTY ASSESSMENT MANUAL are to the 2013 version, which is available at https://www.revenue.wi.gov/Documents/wpam13.pdf.

presumption of correctness, *see* WIS. STAT. § 70.49(2), unless they: (1) conflict with the *Manual* or applicable law; or (2) are rebutted by significant contrary evidence, *see* ***Walgreen/Madison***, 311 Wis. 2d 158, ¶17; ***Great Lakes Quick Lube, LP v. City of Milwaukee***, 2011 WI App 7, ¶14, 331 Wis. 2d 137, 794 N.W.2d 510 (2010). "Whether a city has erroneously failed to follow statutory requirements in making an assessment is a question of law that we review de novo." ***Walgreen/Madison***, 311 Wis. 2d 158, ¶17 (citation omitted).

¶9 The *Manual* and our case law recognize a three-tier methodology for assessing real property. *See* ***id.***, ¶21. First, an assessor considers recent arm's length sales of the property; if available, this is considered "[t]he best evidence of [the property's] fair market value." ***Allright Props., Inc. v. City of Milwaukee***, 2009 WI App 46, ¶21, 317 Wis. 2d 228, 767 N.W.2d 567. However, "[f]or the sale price to be the best information of full value the sale must be made 'under normal conditions' so as to lead to the conclusion that the price paid was that which could 'ordinarily' be obtained for that property." ***Flood v. Village of Lomira, Bd. of Review***, 153 Wis. 2d 428, 437, 451 N.W.2d 422 (1990) (quoting ***State ex rel. Evansville Merc. Assoc. v. Evansville,*** 1 Wis. 2d 40, 43-44, 82 N.W.2d 899 (1957). "When a recent arm's-length sale is available, it is error to consider factors extrinsic to that sale." ***Great Lakes***, 331 Wis. 2d 137, ¶18.

¶10 If there is no suitable recent arm's length sale of the property, an assessor must then "consider sales of 'reasonably comparable' properties." ***Allright Props.***, 317 Wis. 2d 228, ¶22 (quoting WIS. STAT. § 70.32(1)). In order to be considered a "reasonably comparable sale," the compared-to sale must be an arm's length transaction. *See Manual*, 7-25. "Only if there has been no arms-length sale and there are no reasonably comparable sales may an assessor use any of the third-tier assessment methodologies," such as the income and cost

approaches. ***Adams Outdoor Adver., Ltd. v. City of Madison***, 2006 WI 104, ¶34, 294 Wis. 2d 441, 717 N.W.2d 803.

¶11 The circuit court correctly concluded that the City's reliance on the 2009 sale in determining the fair market value of the property was improper. Our supreme court has recognized sale-leaseback transactions are usually "financing tool[s] used by companies to keep capital available for other core business purposes" and that the rental rate in such a transaction "is an amortization over the lease term of the expenses incurred to construct the tenant-specific improvement." ***Walgreen/Madison***, 311 Wis. 2d 158, ¶52. In addition, the International Association of Assessing Officers' (IAAO) Standard on Verification and Adjustment of Sales (2010), which the *Manual* incorporates by reference,[5] notes in Standard 5.9 that "[s]ales involving leasebacks are generally invalid because the sale price is unlikely to represent the market value of the property."

¶12 Given the fact that CVS Pharmacy's rental payments under the lease are tied to the repayment schedule of the property's mortgage—and sales involving leasebacks are generally invalid in valuing real property—we conclude the circuit court properly determined that the sale-leaseback agreement involved unusual financing, thereby inflating the 2009 sale price of the property above market level. *Cf.* ***Walgreen Co. v. City of Oshkosh (Walgreen/Oshkosh)***, No. 2013AP2818, unpublished slip op., ¶¶2, 12-14 (WI App Dec. 17, 2014) (affirming circuit court decision that assessor improperly relied on the Walgreen properties' sale prices because the properties' long-term leases inflated the

[5] *See Manual* 1-3.

properties' values).[6] As such, it did not represent a suitable recent arm's length sale of real property being assessed.[7]

¶13 Relying on ***Great Lakes***, the City appears to argue the circuit court was precluded from finding the sale-leaseback agreement inflated the 2009 sale price above market level because the court improperly ignored CVS Pharmacy's prior admissions—in both a real estate transfer return and the lease—that the 2009 sale's financing is "conventional" and that its lease "is a true lease and does not represent a financing agreement." The City's reliance on ***Great Lakes*** is misplaced. There, in affirming the tax assessments and the circuit court decision, we simply noted that, given the circuit court's factual findings, the taxpayer had failed to "explain why its clear prior admissions of fact [in various documents, such as a real estate transfer return and lease,] should be ignored." ***Great Lakes***, 331 Wis. 2d 137, ¶26. We did not determine that a circuit court is categorically precluded from finding that a sale-leaseback agreement inflated the sale price of a property above market level whenever the real estate transfer return describes the sale's financing as "conventional" or the lease includes language that "it is a true lease and does not represent a financing agreement."

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[6] *See* WIS. STAT. RULE 809.23(3)(b) (unpublished, authored decisions issued on or after July 1, 2009, may be cited for persuasive value).

[7] The League of Wisconsin Municipalities, as amicus curiae, argues the circuit court failed to properly take into account post-***Walgreen Co. v. City of Madison*** (***Walgreen/Madison***), 2008 WI 80, 311 Wis. 2d 158, 752 N.W.2d 687 revisions to the *Manual*. However, to the extent post-***Walgreen/Madison*** revisions to the *Manual* potentially conflict with ***Walgreen/Madison***, courts are required to follow ***Walgreen/Madison***. *See* ***City of West Bend v. Continental IV Fund Ltd. P'ship***, 193 Wis. 2d 481, 487, 535 N.W.2d 24 (Ct. App. 1995) (noting that when a conflict between the *Manual* and common law exists, "common law which accurately reflects the state of the law" controls); *see also* ***Walgreen Co. v. City of Oshkosh*** (***Walgreen/Oshkosh***), No. 2013AP2818, unpublished slip op., ¶14 n.4 (WI App Dec. 17, 2014).

¶14 The City also argues it properly relied on the 2009 sale in assessing the property because the 2009 sale reflected the fair market value in the relevant market—i.e., the investment market for properties subject to triple-net leases with national credit tenants.[8] We disagree. The relevant market is not the investment market for properties subject to triple-net leases with national credit tenants. If that were true, it would invite assessors to impermissibly value "the business concern which may be using the property." ***Walgreen/Madison***, 311 Wis. 2d 158, ¶65 (citation omitted); *see also* ***Walgreen/Oshkosh***, No. 2013AP2818, unpublished slip op., ¶13 ("The problem with the City's argument is that this … restricts the market for Walgreen properties to one that, in the City's own words, includes only 'investment grade real estate' where '[t]he value of the investment is determined by the value of the real estate, the creditworthiness of the tenant and the value of the lease itself.'").

¶15 Moving on to the second-tier of the assessment methodology, the circuit court also correctly concluded that the City's reliance on recent sales of other properties—mostly Walgreens pharmacies—was improper because those properties' long-term leases caused the properties' sale prices to exceed fair market value. By relying solely on recent sales of properties subject to triple-net leases with national credit tenants, the City impermissibly valued "the business

[8] Citing ***State ex rel. N/S Assoc. v. Board of Review***, 164 Wis. 2d 31, 473 N.W.2d 554 (Ct. App. 1991), the City also argues the circuit court erred in concluding there were "problems with the openness of the market" the CVS Pharmacy property was sold in simply because the property was sold in a specialized investment market. However, we need not address this argument because, even assuming this argument has merit, it would not change our conclusion that the City's reliance on the 2009 sale in determining the fair market value of the property was erroneous since the sale-leaseback agreement involved unusual financing, thereby inflating the 2009 sales price of the property above market level. *See* ***Turner v. Taylor***, 2003 WI App 256, ¶1 n.1, 268 Wis. 2d 628, 673 N.W.2d 716 (appellate courts need not address every issue raised by the parties when one is dispositive).

concern which may be using the property." ***Walgreen/Madison***, 311 Wis. 2d 158, ¶65 (citation omitted); *accord* ***Walgreen/Oshkosh***, No. 2013AP2818, unpublished slip op., ¶13 ("[T]he market does not value a property without Walgreen as a tenant as highly as it does a property where Walgreen remains a tenant subject to a long-term lease.").

¶16 The City appears to argue the circuit court improperly limited the comparable sales and leases the City could consider in valuing CVS Pharmacy's property to "the local Appleton market," citing the court's statement that the City's second-tier assessment methodology failed to "take [CVS Pharmacy's] property out of the investment market and bring it into the Appleton real estate market." Stripped of context, the court's isolated statement may appear problematic, as assessors ordinarily have a duty to *consider* sales of comparable properties outside their locality. *See Manual*, 9-6 ("[F]or many properties, the assessor must look outside of the municipal boundaries for comparable property types and uses to find similar sales and leases.").

¶17 Prior to the circuit court's statement with which the City takes issue, the court wrote the City is "valuing the subject property, not based on its use as a pharmacy/drug store, but as a triple-net lease investment opportunity." The court then concluded the City "is to assess the property located in the city, not the creditworthiness of tenants occupying that property." Viewed in its proper context, the court did not impermissibly limit the comparable sales and leases the City could consider in valuing CVS Pharmacy's property to the local Appleton market. Rather, the court was explaining how the City's second-tier assessment methodology—which defined the property's highest and best use as a pharmacy/drug store subject to a triple-net lease with a national credit tenant—failed to comply with ***Walgreen/Madison***'s command that assessors "value the

real estate [itself], not the business concern which may be using the property." ***Walgreen/Madison***, 311 Wis. 2d 158, ¶65 (citation omitted).

¶18 The circuit court also correctly determined that the City's reliance on CVS Pharmacy's contract rents when utilizing the income approach was improper because those rents were above market. The City asserts that "[t]here is no evidence in the record that the rents are not at market." However, given the sale-leaseback agreement—which involved unusual financing—the circuit court properly concluded that the contract rents did "not provide a reliable indication of market rent." ***Walgreen/Madison***, 311 Wis. 2d 158, ¶57.

¶19 Finally, the circuit court correctly concluded that the City's reliance on the property's 2008 purchase price of $1,975,000 to value the land when utilizing the cost approach was improper because CVS Pharmacy presented significant contrary evidence. In valuing the land (as opposed to the entire property) under the cost approach, the City relied solely on the property's 2008 purchase price—which reflected the 2008 value of the *entire* property (i.e., the land *and* an existing building). In contrast, CVS Pharmacy presented significant contrary evidence showing that the land (as opposed to the entire property) was worth between $470,000 and $535,000 on the post-2008 assessment dates; this value was verified by comparing it to the 2012 sale of land adjoining the property at issue. Utilizing the cost approach, Mike MaRous, one of CVS Pharmacy's expert witnesses, valued the entire property at $1,690,000 for 2011; $1,760,000 for 2012; and $1,855,000 for 2013.

¶20 Since the City's assessments violate the principles set forth in ***Walgreen/Madison***, and CVS Pharmacy presented significant contrary evidence rebutting the assessments, the circuit court properly concluded that the

assessments are not entitled to a presumption of correctness. Relying on the testimony of CVS Pharmacy's experts, the court then concluded that the property's value was $1,690,000 in 2011; $1,760,000 in 2012; and $1,855,000 in 2013.

¶21 Finally, the City argues the circuit court's valuations are erroneous because it utilized the cost approach, rather than the comparable sales approach, to reach its valuations.[9] The circuit court utilized the cost approach to value the property. However, it also compared the property's (per square foot) value to the (per square foot) value of a Walgreens store, and found the values to be comparable. In light of the fact that the court's valuations were within the ranges introduced by CVS Pharmacy's expert witnesses, *see* ***Bloomer Housing***, 257 Wis. 2d 883, ¶12 (fact-finder ultimate arbiter of expert witness testimony), and that the court cross-checked its valuation by comparing it to the valuation of a comparable property we previously affirmed, *see* ***Walgreen/Oshkosh***, No. 2013AP2818, unpublished slip op., ¶¶2, 7, 14-15, we conclude that the circuit court's valuations are not clearly erroneous.

[9] Citing ***Nestlé USA, Inc. v. DOR***, 2011 WI 4, 331 Wis. 2d 256, 795 N.W.2d 46, the City also appears to argue the circuit court's valuations are erroneous because the court relied on the assessments of CVS Pharmacy's expert witnesses classifying the property's "highest and best use" as a general retail establishment, rather than as a pharmacy/drug store. Devoid of context, portions of the circuit court's decision could be interpreted to support the City's argument. However, the court was explicit that it was *not* classifying the property's "highest and best use" as general retail when valuing the property. As the court stated in its written decision: "Given the difference between the [property] as a *pharmacy drugstore* and most of [CVS Pharmacy's] comparables as *general retail properties*, the Court finds that the cost approach provides the most reliable indication of value and should be given more weight. … This valuation … is similar to other recent court-determined valuations of *retail pharmacies* in the Fox Valley." (Emphasis added.)

By the Court.—Judgment affirmed.

This opinion will not be published. *See* WIS. STAT. RULE 809.23(1)(b)5.