

Value Transfers: Implications of the *Federated* Decision

MAAO

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Federated Retail Holdings, Inc. v. County of Ramsey, 820 N.W.2d 553 (Minn., 2012).

- **Background:** Taxpayer sought review of county tax assessor's valuation of the Macys department store property at Rosedale Mall.
- The Tax Court, [2011 WL 4537074](#), found that taxpayer's ownership interest in the department store included the leasehold interest in adjacent property, but concluded that the value of the leasehold interest was not subject to the jurisdiction of the tax court and therefore did not include it in the valuation. County petitioned for writ of certiorari.

Holdings:

- Upon grant of certiorari, the Supreme Court, Dietzen, J., held that:
- (1) tax court had subject-matter jurisdiction over taxpayer's leasehold interest in property that was adjacent and contiguous to the tax parcel, and
- (2) “Parcel 0004’s leasehold interest to the exclusive use of the basement space of Parcel 0005 is an interest in real property that satisfies the criteria of a covenant that runs with the land, and therefore is a right or privilege that belongs or appertains to the land within the meaning of Minn. Stat. § 272.03, subd. 1. Consequently, its contributory value as an integrated part of that department store is properly included in assessing all factors that contribute to the value of the tax parcel on appeal.”
- Reversed and remanded.

Assessment History of the Property

- Impact of Mall of America on existing malls and actions taken by Rosedale and Dayton's
 - The looming construction of the Mall of America caused the mall owner to strengthen their market position by locking Dayton's Department stores (*the dominant anchor in the MSP market at that time*) into long term leases at both Rosedale and Southdale Malls.
 - The Rosedale Mall deal included the construction of a new store for Dayton's at Rosedale, with the mall absorbing the original Dayton's department store space into the remodeled mall.
 - However, the basement of the original store was retained by Dayton's under a long term lease, and made part of the new Dayton's store.

Federated (Macy's Rosedale)

Property Tax Case

- **ISSUES:** Does the Court have Subject Matter Jurisdiction over the adjacent leased premises located on a separate tax parcel and should its value be included in assessing the value of the department store?
- **HOLDING:** Yes, if the leasehold interest constitutes a right or privilege belonging or appertaining to the subject tax parcel and if it affects the fair market value of the tax parcel

Macy's Rosedale

- 09.223.42.0004

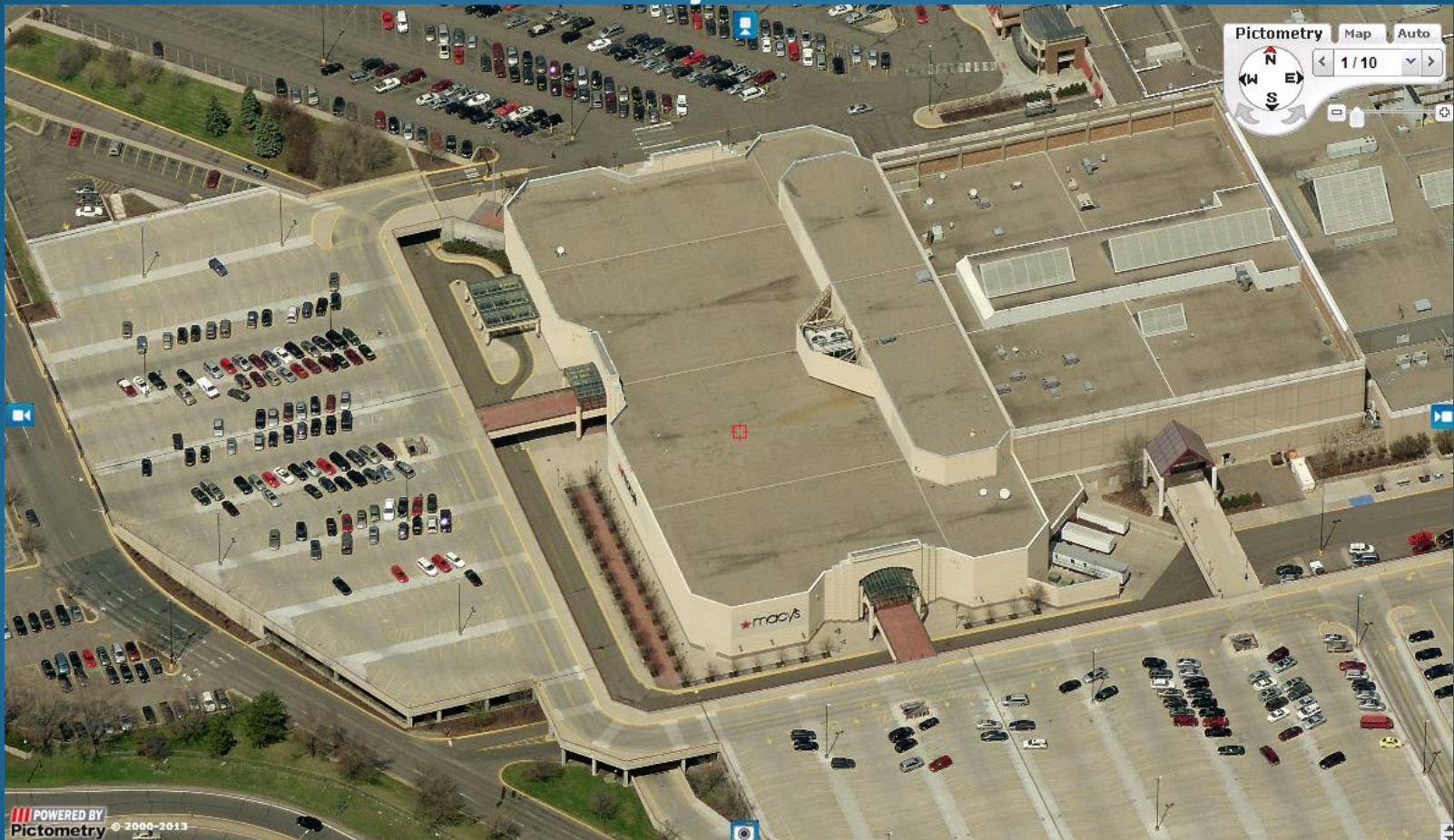
- Store GLA - 259,453 [//]
- Owned GLA - 214,017 [//]
- Leased GLA - 45,436 [//]

- Original Assessed values: 2006 and 2007 \$17,000,00
- Tax Court Value 2007 \$15,245,024 less lease \$12,575,281
- Final Settlement 2007 after Remand \$14,500,000

Photo of Rosedale



Photo of New and Old Rosedale Macys



Assessment of leased space

- The mall owners and Dayton's property tax officials requested the leased basement department store area be assessed as part of the Dayton's store parcel. Therefore, this department store space, located under the first level of Rosedale mall and physically part of the mall parcel was not taxed as part of the mall, but rather as part of the Macys store. This practice began in 1992 and continued through the assessment years under appeal.
- Assessment of the basement department store space on the Macys parcel eliminated the need for the Mall owner to calculate or bill Dayton's/Macy's for a pro rata share of the mall property taxes since this allocation has already been performed by the assessor when the assessment was certified.

Lease Terms

- Premises: 45,436 square feet
- Use restricted to “an integrated part of the operation of Tenant’s department store operated adjacent to the Premises ... including but not limited to selling and display area, office, storage and employee facilities.”
- Rent: \$1.00 per annum payable annually.

Lease Terms

- **Term:** 15 years with the option of extending the term for up to 100 additional periods of one year each. Each such extension shall be automatically exercised subject to certain conditions, among which was the requirement that at the beginning of each one year extension the Premises and the Main Store are being operated as a fashion oriented retail department store under an approved name.
- **Successors:** The Lease, and the covenants and conditions in it, “shall inure to the benefit of and be binding upon Landlord, its heirs, executors, administrators, successors, and assigns, and shall be binding upon Tenant, its heirs, executors, administrators, successors, and assigns, and shall inure to the benefit of Tenant and assigns of Tenant.

Subsequent assignments of lease

- Dayton's sale to May Department Stores Company
- May becomes Federated Retail Holdings

Definition of Real Property

- These are *in rem* proceedings. The definition of the *res* is crucial, and is found in the definition of Real Property in **Minn. Stat. § 272.03**:
- **“Subdivision 1. Real property. (a) For the purposes of taxation, “real property” includes the land itself, rails, ties, and other track materials annexed to the land, and all buildings, structures, and improvements or other fixtures on it, bridges of bridge companies, and all rights and privileges belonging or appertaining to the land, and all mines, iron ore and taconite minerals not otherwise exempt, quarries, fossils, and trees on or under it.”**



Previous Cases

- *The Rule in Spencer's Case* (1583)
- *The Rule in Spencer's Case* is alive and well. It distinguishes between a right or privilege belonging or appertaining to the land and a personal right or obligation. If the right “belongs or appertains to the land” it is said to “run with the land.”

Pelser v. Gingold, 214 Minn. 281, 8 N.W.2d 36 (1943)

“A covenant is said to run with the land when it touches or concerns the land granted or demised ... As the term implies, the covenant must concern the occupation or enjoyment of the land granted or demised and the liability to perform it, and the right to take advantage of it must pass to the assignee.” 214 Minn. at 285, 8 N.W.2d at 39.

“A covenant that runs with the land is a contractual obligation with certain real characteristics, such that it attaches to land rather than being a personal obligation of the grantor.” *Ibid.*

Alvin v. Johnson, 241 Minn. 257, 63 N.W.2d 22 (1954)

- **Applied to easements:** “Because easements affect the value of the benefitted and burdened property, we concluded that easements are part of the property rights assessed and therefore not extinguished by the tax deed.” 241 Minn. at 263, 63 N.W.2d at 27.
- **Effect on Value:** “Appurtenant easements are factors definitely affecting values. When the assessment of what is now the Nordquist property was made in 1926, one of the elements and factors which the assessor under his duty was required to take into consideration was the fact that the property was burdened with an easement which materially reduced the value of the property; and in assessing the plaintiffs' property, it was the assessor's duty to take into consideration the additional value the property had by reason of the easement appurtenant. Taking that into consideration, naturally, a higher value would be found to exist. The value of the easement influenced the valuation placed upon the dominant tenement. In 3 Cooley, Taxation (4 ed.) s 1154, the author states: “* * * The servient estate must be assessed at its value subject to the easements and the dominant estate at its value with the easements.” 241 Minn. at 262, 63 N.W.2d at 25.

Other jurisdictions

- *County of Du Page v. Property Tax Appeal Board*, 303 Ill.App.3d 538, 708 N.E.2d 525, 236 Ill.Dec. 939 (1999).
- The value of a department store on a leased pad site was *not* diminished because the parking area, to which it had access by the terms of its lease, was on a separate parcel not being valued. The parking rights under lease are factors in its value under a statutory definition of real property as the land itself and “all rights and privileges belonging or pertaining thereto.”



Additional Decision

- *Meritex Enterprises, Inc. v. County of Ramsey*, File No. CX-06-4506, 2009 WL 2366285 (Minn. Tax Ct. July 24, 2009)
- Parking easement: “We agree with Respondent that property benefitted by an easement interest has added value, whereas the burdened property loses value from it.” *Meritex* at *9.

Covenants that “Run with the Land”

- *Federated Retail Holdings, Inc. v. County of Ramsey*, 820 N.W.2d 553 (Minn. 2012)

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- A covenant in a lease “runs with the land” if

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- The parties are in privity of estate when the covenant is made,
- The covenant touches and concerns the land, and
- The liability or right that runs with the land is assignable and has validly been assigned.

AND

- The contributory value of the space that “runs with the land” must be included in assessing the value of the department store because, based on **Minn. Stat. § 273.12**: “It shall be the duty of every assessor and board, in estimating and determining the value of lands for the purpose of taxation, to consider and give due weight to every element and factor affecting the market value thereof ...”

Implications for Assessors

- A need to determine if there has been a value transfer because of a right that runs with the land.
- The parcel description describes **ONLY** the real estate. But since we assess and the tax real property we must look further.
 - **Real Estate** is the land and all attachments on, below or above the land surface.
 - **Real Property** also includes all rights and privileges belonging to or appertaining to the land..

Definition of the Real Property Appraised

- The Fee Simple Estate includes ownership of ALL rights in a property except those retained by the government. Therefore, Minnesota assessors value and assess the total of all real property associated with each tax parcel of real estate.
- The 13th Edition of the Appraisal of Real Estate Page 115 states: “Under the Bundle of Rights theory a contract does not change the Bundle of Rights, but may constitute an encumbrance that affects the value of real property.”

Why would or should an assessed value be calculated in this manner?

- Why does this “transfer” of assessed value make sense?
 - To allocate the value of real estate/real property transferred to a benefitting property when certain covenants exist via an easement or lease.
 - To allow the assessor to overcome a situation which would otherwise result in an “omitted value”. This assessment situation could mean the “transferred” value would otherwise not be identified, and would not be valued as part of either parcel.
 - By properly identifying and listing the “transferred” value on the assessment of the benefitting parcel all value requiring assessment may then be correctly captured.

When should an assessor consider assigning this value to the dominant parcel?

- If a right transfers automatically to future owners with a nominal or zero payment.
- If the right transferred relates to the use or occupancy of the property
- If there is a written agreement specifying the terms of the covenant; it could be an easement, a lease, an operating agreement, etc. The form is not controlling
- If these characteristics are present, consult with your County Attorney. The transferred rights may “run with the land”.

Concerns

- Double taxation - this must be analyzed and avoided
- Confusion - Clear communication is required between the assessor and the owner/ taxpayers of parcels where their property assessment has been impacted by inclusion of the effects of a covenant created by an easement or lease.
- Proper Care – The Assessor must take care to deduct the loss in value to the servient property. This loss in value does not necessarily equal the increase in value to the dominate parcel, but it may.
- Legal Justification - Has the assessor properly consulted with his/her County Attorney over the questions relating to the existence of a “qualifying” covenant.

Final Resolution

- Remand Decision by Supreme Court included language instructing court to add back the “Leased Fee” value of the leased basement space.
- Taxpayer argued for very low value - much lower than the value the Tax Court Deducted
- Language confused the issue of pure “Leased Fee” and the “Fee Simple” interest of leased space.
- County: Valuation of the contributory value of the leased space is NOT the same thing as valuing the Leased Fee interest of rights that do not “run with the land”.