Pierce County
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Office of Assessor-Treasurer

2010 Commercial & Industrial Valuation Summary

A general overview of the methodology used by the Commercial Team to establish assessed values for Assessment Year 2010.

TABLE OF CONTENTS

Commercial & Industrial Valuation Summary

INTRODUCTION

This document is designed to aid in the understanding of the assessed values placed on commercial property in Pierce County. It is not intended to serve as an all-encompassing document, but rather as a summary to give a general understanding of the origin of our assessments. The reader is encouraged to pay particular attention to the section titled "Approaches to Value", as it explains the basic framework for this entire process.

Commercial or income producing real estate is typically purchased as an investment, from an investor's point of view. **Earning power** is the critical element affecting property value. The basic premise holds that the higher the expected earnings, the higher the value, given similar risk. The indication of value from an i*ncome approach* is paramount where adequate data presents itself, however, many properties must be valued using other techniques. Properties without adequate income data were appraised using either the *sales comparison* or the *cost approach* to value. In this report we will summarize the process used to produce a value using these three approaches to value.

A brief summary of the appraisal process is included, as well as a limited discussion of the techniques utilized to address land values and the effect "excess" land may have on a valuation assignment. We will also give you our understanding of the Uniform Standards of Professional Practice (USPAP), and how they affect our valuations.

UNIFORM STANDARDS

The valuation process used for real property in Pierce County is based on a compilation of requirements from legal and professional appraisal perspectives. The legal perspectives are based on state law, precedent setting case law, rules and regulations, and published opinions from the Washington State Department of Revenue.

Professional appraisal standards, known as the Uniform Standards of Professional Appraisal Practice (USPAP), are published by the Appraisal Foundation, and promoted by each state. The Appraisal Foundation, a private organization comprised of nine professional appraisal organizations, was formed in 1987 for the purpose of promulgating uniform standards for appraisers. The organization that represents assessors in the Appraisal Foundation is the “International Association of Assessing Officers” (IAAO). The standards provided by the Foundation entail the framework from which all appraisals should be conducted.

Since our specific focus within these standards is the valuation of real property for *ad valorem* tax purposes, primary emphasis is given to Standard 6 on Mass Appraisal. However, due to the existence of many "unique” properties within Pierce County, individual property appraisal standards are also necessary. Mass appraisal and individual property appraisal standards are logically similar. Each complements the other, in that each is intended to produce credible results reported in an understandable format, by competent individuals.

These uniform standards specifically require that the appraiser act as a disinterested third party; that the valuation assignments be performed with unbiased impartiality, objectively and independent, without accommodations of personal interests.

It is the intention of this department to meet the requirements of The Uniform Standards of Professional Appraisal Practice, specifically Standard Six. The Pierce County Assessor~Treasurer exercises the right to limit the scope of work where necessary, due to limitations placed on our appraisals by legally binding court decisions, state law, published opinions by the Washington State Department of Revenue and economic or administrative influences.

APPROACHES TO VALUE

Commercial property appraised and evaluated through the application of appraisal techniques using the three approaches to value (i.e., cost approach, sales comparison, and income capitalization). Each one of these techniques derives separate indications of value for the property. When adequate data is available, all three approaches to value should be considered. Therefore, where appropriate, the valuation process must collect, verify, analyze, and reconcile the information necessary to estimate: (a) the replacement (or reproduction) cost of the improvements; (b) the accrued depreciation; (c) the value by the sales of comparable properties; and (d) the rent(s), expenses, capitalization rates and vacancy rates necessary to value the property by the income capitalization approach. The valuation process must consider factors that affect supply and demand. Existing land use regulations, neighborhood trends, and the physical adaptability of the property to the most probable use are just a few.

The Cost Approach is a set of procedures through which a value indication is derived by estimating the current cost to construct a reproduction of, or a replacement for, the existing structure plus any profit or incentive; deducting depreciation from the total cost, and adding the estimated land value.

The Sales Comparison Approach is a set of procedures in which a value indication is derived by comparing the property being appraised to similar properties that have been sold recently, applying appropriate units of comparison, and making adjustments to the sale prices of the comparables based on the elements of comparison.

The Income Approach utilizes a property's capacity to generate future benefits and capitalize them into an indication of value. The principle of anticipation is fundamental to this approach. Rental income is estimated from market data, reduced for typical loss to vacancy and expenses, and capitalized by a rate an investor would use.

The Income Approach Pierce County typically uses, is called direct capitalization. Direct Capitalization is used to convert a single year's income expectancy into an indication of value in one direct step by dividing the income estimate by an appropriate rate. Under some circumstances the appraiser may consider more than one year's income to eliminate some of the cyclical influence that may cause a valuation to fluctuate. We call this income stabilization.

The ultimate goal of the valuation process is a sound conclusion of value. This requires a reconciliation of the value indications derived from the different approaches. Consideration should be given to the relevance of the approach and the reliability of the value indication based on the quantity and quality of data. A single market transaction (i.e., sale price), or actual construction cost, or capitalized income stream for a specific property cannot be assumed to be market value. These are indications of an agreement between one buyer and one seller on the value in exchange for one particular property. While the indication may estimate market value, it should be supported by other indications of market value. Therefore, the quantity of data and the dispersion in value indications is critically important.

Use of multiple independent approaches to value that result in closely clustered values is usually a sign of sound value conclusions. When value indications are substantially different, careful analysis of the valuation data used and the assumptions made is needed to determine which value indicator is the most reliable.

LAND VALUATION

Deriving a land value estimate is an essential element of applying the three approaches to value. While the income approach is most often used, the cost and sales comparison approach also require an understanding of land value, and expected land requirements.

Land value is typically derived from sales of similar properties and compared either on a square foot or unit basis. Sales are analyzed and appropriate adjustments are derived from the available data.

Pierce County also develops land models by using regression analysis to calibrate the influence factors for characteristics such as size, location and allowable use, to name a few. Appraisers apply the models and in some cases further adjust the value estimate for specific influences that are underrepresented in the data used to build the model.

Utilizing the income and sales comparison approach requires an understanding of the necessary land to support the business. The expected land area to building area is based on densities and parking ratios that jurisdictions require. Additional land area not needed to support the business is not typically capitalized in the rent being paid, nor present in the comparables used. An estimated value of the “excess” land must be added to the value derived from the income, and sales comparison approach.

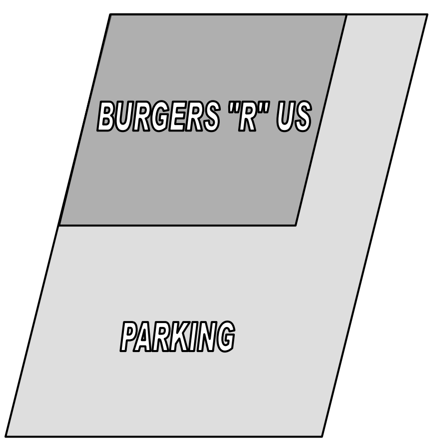
The cost approach does not require the use of land to building ratios. In the cost approach the land value is established separately, and added to the depreciated value of the improvements. Additional adjustments to the cost approach for factors affecting value, such as functional or economic obsolescence, are made to arrive at a final estimate of value.

To better understand the concepts that affect the sales comparison and income approaches, an example has been provided below. In this example imagine that "Burgers R Us" is paying rent for the use of the building and the "typical" land area. Burgers R Us is not going to pay additional rent for excess land when they only need enough land for their customers to park, therefore the rent and estimated value from the rent does not include the value of the excess land. As you can see, there are options that example B has that A doesn't. In example B the owner could expand, or possibly segregate off a portion of the land to sell. The excess land has value independent to the income stream. Therefore, excess land value must be estimated and added to the value estimate indicated by the income approach.

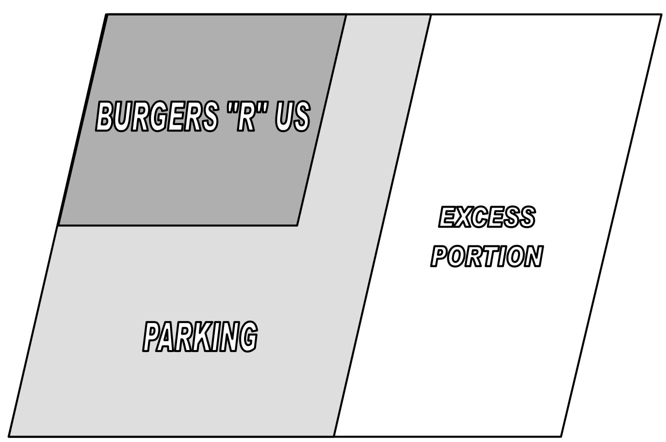
If ground rent data is available, the appraiser may also choose to estimate the income to the excess land and capitalize its net operating income. In this process the capitalization rate would be lowered to include only the return on investment and the effective tax rate.

The sales comparison approach can be similarly understood. In applying a sales comparison approach most comparables are going to have typical land to building ratios. When the subject is like example B with excess land, the value of the land must be estimated separately and added to the value indicated through the sales comparison approach.

Note: If the sales are all comparable to the subject, in that they also have excess land, similar in value to the subject, the statement above would not be true. You would not need to adjust for the excess land if the sales comparables were similarly affected.



Site "A"
Typical Land to Building Ratio



Site "B"
More than Typical Land to Building Ratio

LAND TO BUILDING RATIOS

Land to building ratios vary from jurisdiction to jurisdiction based on the use of the property. We have provided typical ranges for these ratios that we expect to see throughout the County.

Land: Building Ratios

Apartments	1.5 - 2 : 1
Banks/Neighborhood	4 - 5 : 1
Banks/High Volume	7 : 1
Offices	2 - 3 : 1
Restaurants	10 : 1
Warehouses	2.5 - 4 : 1
Whse Light Ind	4 : 1

Retail

Regional (Use Code 5380)	4 – 5 : 1	ie: Tacoma Mall
Community (Use Code 5370)	3.5:1	ie: Narrows Plaza; Westgate
Neighborhood (Use Code 5360)	3:1	ie: Green Firs
Retail (Use Code 5395)	4:1	ie: All other miscellaneous

Example: A 5,000 square foot Restaurant would typically have at least 50,000 square feet of land.

PARKING TO BUILDING RATIOS FOR SHOPPING CENTERS

BUILDING AREA	TYPICAL PARKING REQUIREMENT
25,000 – 400,000 SF of GLA	4 spaces per 1,000 SF of GLA
400,000 – 600,000 SF of GLA	4.5 spaces per 1,000 SF of GLA
600,000 + SF of GLA	5 spaces per 1,000 SF of GLA

CONCLUSION

The concept of market value is of paramount importance to business and real estate communities. Vast sums of debt and equity capital are committed each year to real estate investments and mortgage loans, which are based on market value estimates. Real estate taxation, litigation and legislation also reflect an ongoing, active concern with market value issues. In virtually every aspect of the real estate industry and in its regulation at local, state and federal levels, market value considerations are of vital importance and essential to our nation's economic stability.

The definition of market value must be clearly understood and communicated. Careful distinction must be made between the concepts of *price* and that of *market* value. The term *price* usually refers to a given sale or transaction. It implies an exchange; a price is an accomplished fact. Once finalized, it represents the amount a particular purchaser agreed to pay a particular seller under the circumstances surrounding their transaction. A real estate *market*, on the other hand, is the interaction of a number of individuals on a number of competing transactions. No clear conclusions can be drawn regarding the appropriateness of a given price, without looking at multiple transactions of similar properties within the same market.

Along these same lines, the temptation to apply inordinate weight to one particular approach to value, while underestimating the indicated results achieved through competing valuation techniques, should be avoided. It is only through a reasoned analysis that encompasses all the appropriate approaches to value that reasonable value conclusions can be achieved.

REFERENCES

- Appraisal Institute, The Appraisal Of Real Estate Twelfth Edition, 2001 Appraisal Institute
- The International Association of Assessing Officers, Property Appraisal And Assessment Administration, 1990 The International Association of Assessing Officers
- New York State, Assessor's Manual, 2002 New York State, Office of Real Property Services

Statistical Summary Report for the 2010 Commercial Revaluation

Introduction

The 2010 Commercial Revaluation Report is presented to assist Assessor-Treasurer staff in answering questions regarding assessed value changes on commercial/industrial property in Pierce County. It also assists the County Board of Equalization in understanding the 2010 value changes. The report includes a summary of the revaluation process, a sales trend report, sales ratio statistics, a value change report and a sales listing by use group. Assessed values reported are as of January 1st, 2010.

Valuation Standards

For ad valorem tax purposes, the Pierce County Assessor-Treasurer is required by law to annually list all property as of January 1st of each year, at one hundred percent of the true and fair market value of land and improvements. County assessors are authorized to place any property that increased in value due to new construction on the assessment rolls up to August 31st of each year and the value shall consider the characteristics of the property as of July 31st of that year.

Mass appraisal standards are used to establish assessed values. The definition of Mass appraisal is "the process of valuing a group of properties as of a given date, using standard methods, and allowing for statistical testing"[1]. Sales from the previous year(s) are statistically analyzed to establish new land and improvement values and evaluate the accuracy of the assessments.

Property Records

Property assessment characteristic records are maintained for all properties in Pierce County. These records are established when parcels or improvements are initially added to the assessment rolls. Characteristics such as building square footage, style, quality and condition are used to establish improvement records. Improvement records usually include sketches of buildings and photos. Characteristics such as land size, amenities, and functional issues are collected to establish land records. Pierce County is on a six year physical inspection cycle, meaning one sixth of the county is subject to physical inspection each year. During the physical inspection cycle, an appraiser observes the property and verifies that the assessor's property characteristic data is accurate. When changes are made to pertinent characteristics (examples: new construction, condition changes, demolition, etc.) the property is reappraised.

[1] Source: Property Assessment and Administration; The International Association of Assessing Officers; Editors, Joseph K. Eckert, PH.D, Robert J. Gloudemans & Richard R Almy

Location Analysis

Commercial sales data is stratified into three primary categories for the purpose of market trend and sales analysis.

First:

- The County is divided into 9 geographical market areas/neighborhoods.
- The location of each commercial market area/neighborhood is shown on the map following this document.
- The areas listed are Tacoma North, Tacoma South, Tacoma CDB, Tacoma Port, Peninsula, North County, East County, West County, and Central County.
- These market areas are further divided into 48 sub neighborhoods for valuation purposes.

Second:

- Commercial land is stratified by LEA (Land Economic Area), and land use; Multiple Unit, Commercial, Commercial Other, and Industrial.
- LEAs are used for land sale analysis and application of land valuation models.
- The Tacoma Central Business District (CBD) has five LEAs developed based on neighborhood zoning, land use, and location.

Third:

- Commercial improvements are stratified by specific use groups like Retail, Office, or General Warehousing.
- Analysis by location and use group allows the Assessor to isolate the physical, economic, governmental, and social factors that affect the real estate market.

Statistical Trend

The county is on a six year physical inspection cycle, with 1/6th of the county being subject to physical inspection each year. The 5/6th not physically inspected, is statistically updated, or "trended". This trend is developed from sales ratios. The ratio of assessed value to sale price (AV÷SP) provides the information needed to determine the accuracy of the assessed values. Sales ratio analysis is done by adjusting the land and building assessed values of sold properties until an acceptable level and uniformity of the sales ratios is achieved. Reports included in this book indicate the quality of the assessment and are broken into several categories based on location and use.

Valuation Models

The commercial team physically inspects 1/6th of the county each year. The statistical team supports this effort by providing generic land, cost and income models that appraisers use to begin their valuation of each property. Models are simply mathematical formulas that replicate changes in value based on property characteristics. A model can be a set of cost tables or a complex formula derived using multiple regression analysis. The goal is to create tools that appraisers can use to quickly estimate value for various properties.

Land Valuation

Commercial land models developed from sales in the same use category are referred to as Land Economic Areas (LEAs). For example: Sales of industrial land are analyzed together from across the county to develop a model for industrial land. Commercial sales are used for commercial models and so on. Basic formulas that estimate value based on size and location are developed for each of these uses. Adjustments are then developed for characteristics such as shape, topography, busy street etc.

Appraisers use these models as a starting place. The model gives them general direction as to the influences in the market and how they affect value. The appraiser makes further adjustments to account for additional influences that are not defined in the model or are not "average" or typical for the area.

Cost Approach

The majority of commercial properties in Pierce County are valued by a market adjusted cost approach. The cost approach begins with a replacement cost new for the improvements. Depreciation is then subtracted for physical wear and tear and for functional or economic obsolescence. The land value is then added to the depreciated value of the improvements to arrive at the total value of the property.

Marshall & Swift cost rates provided by the CAMA software vendor are utilized as the basis for the cost approach[2]. The statistical team makes changes in the rate tables to calibrate the cost rates to our Pierce County market using Marshall & Swift Cost Multipliers and local sales in the Pierce County market area.

Market Approach

The market or sales comparison approach is the process of developing valuation criteria from sales of comparable properties and applying it to the subject property(s). Private appraisers commonly rely on this approach for single family appraisal. In mass appraisal sales can be used to develop models or calibrate cost tables.

Pierce County uses a market adjusted cost approach for most properties. This process seeks to replicate the results from individual appraisals as in the private appraisal industry. Appraisers may use value indications ($ per square foot or unit) when appraising the 1/6th of the county in the physical inspection area, but they will use these indications to help guide them in making adjustments to the cost or income approach.

It is important to note that the Pierce County Assessor Treasurer converted property characteristics from the legacy CAMA system into the current system in March of 2003. Commercial values from the legacy system were converted into the new CAMA system

[2] Marshall and Swift cost rates are provided with our Computer Assisted Mass Appraisal (CAMA) system, by the vendor, Colorado Custom Ware, Inc. Marshall and Swift is a nationally recognized provider of cost rates for the appraisal industry.

as “Market Override Values”. When properties are inspected or reviewed by the Commercial Team, market override values from the legacy system are removed and replaced by a market adjusted cost or income model valuation. Properties remaining on market override for the 2010 assessment year are trended to January 1st market values.

Income Approach

The income approach is applied by the commercial team in a uniform manner using models developed for specific property types. The Statistical team has developed base income models for Retail, Apartments, Office, and Warehouse property types. These models are developed from income and expense statements, data we are provided during appeals and third party data we purchase.

As in the land valuation and the cost approach, these income models provide a starting place for the commercial appraiser. There are many influences in the market that are not represented in the data we analyzed to create the model, so the commercial appraiser must adjust these models for specific influences such as location or access. Adjustments to the base income model result in override income models which are trended annually based on sales ratio analysis.

2010 Revaluation Summary Statistics and Value Change Report

Summary ratio statistics and assessed value percent change reports are provided in the following sections of this book. The ratio statistics include two years of sales (2008 and 2009). The assessed value change report shows average value change statistics from 2009 to 2010 by neighborhood, city and school district.