ATTORNEY FOR PETITIONER:
**BRADLEY J. ADAMSKY**
NEWBY LEWIS KAMINSKI & JONES, LLP
LaPorte, IN

ATTORNEY FOR RESPONDENTS:
**MARILYN S. MEIGHEN**
MEIGHEN & ASSOCIATES, PC
Carmel, IN



# IN THE INDIANA TAX COURT

| | | |
|---|---|---|
| COUNTRY ACRES LIMITED PARTNERSHIP, | ) | |
| | ) | |
| Petitioner, | ) | |
| | ) | |
| v. | ) | Cause No. 71T10-0903-TA-5 |
| | ) | |
| PLEASANT TOWNSHIP ASSESSOR, | ) | |
| and LAPORTE COUNTY ASSESSOR, | ) | |
| | ) | |
| Respondents. | ) | |

ON APPEAL FROM THE FINAL DETERMINATION
OF THE INDIANA BOARD OF TAX REVIEW

**NOT FOR PUBLICATION**
**July 19, 2010**

FISHER, J.

Country Acres Limited Partnership (Country Acres) appeals the final determination of the Indiana Board of Tax Review (Indiana Board) valuing its commercial property for the 2004 tax year. The issue for the Court to decide is whether the Indiana Board erred in valuing the property.

## RELEVANT FACTS AND PROCEDURAL HISTORY

During the 2004 tax year, Country Acres owned a ten-building, garden-style apartment complex in LaPorte, Indiana. The one-hundred unit complex, constructed in

1972, was primarily occupied by "Section 8" tenants and was situated on approximately seven acres of land.[1] (*See* Cert. Admin. R. at 97-107, 266-67 (footnote added).)

For the 2004 tax year, the Pleasant Township Assessor/LaPorte County Assessor (collectively, the Assessor) assessed Country Acres' complex at $3,336,200. Believing that value to be too high, Country Acres appealed the assessment, first to the LaPorte County Property Tax Assessment Board of Appeals, and then to the Indiana Board.

On October 21, 2008, the Indiana Board conducted a hearing on matter. During the course of those proceedings, Country Acres presented two analyses to demonstrate that its assessment was incorrect. The first analysis, an "appeal summary" prepared by Mr. Robert Porter (an Indiana certified Level II assessor-appraiser), estimated that as of January 1, 1999, the property's market value-in-use was $836,921.[2] Porter's analysis

[1] The United States Department of Housing and Urban Development (HUD) operates a subsidized housing program for low-income families and individuals commonly known as "Section 8." Under this program, HUD determines the amount of rent that a landlord may collect from its tenants. A tenant's actual rent liability is based on his/her income; HUD makes up any shortfall. (*See* Cert. Admin. R. at 27, 326-28.)

[2] Indiana assesses real property on the basis of its "market value-in-use." *See* IND. CODE ANN. § 6-1.1-31-6(c) (West 2004); 2002 REAL PROPERTY ASSESSMENT MANUAL (2004 Reprint) (hereinafter, "Manual") (incorporated by reference at 50 IND. ADMIN. CODE 2.3-1-2 (2002 Supp.)) at 2. A property's market value-in-use (i.e., the value of the property "for its current use, as reflected by the utility received by the owner or a similar user, from the property") may be ascertained through the application of the cost approach, the sales comparison approach, or the income approach. Manual at 2, 3. Indiana's 2004 assessments were to reflect a property's market value-in-use as of January 1, 1999. *See id.* at 4, 8.

utilized the income approach to value.[3] Country Acres' second analysis, an appraisal completed in conformance with the Uniform Standards of Professional Appraisal Practice (USPAP), was prepared by Ms. Janet Sallander (a certified member of the Appraisal Institute) of Cushman & Wakefield of Illinois, Inc. (hereinafter, "C&W") for First Bank of Beverly Hills. The C&W appraisal, which also employed the income approach, estimated that the market value of Country Acres' complex was $2,200,000 on June 28,

[3] Under the income approach, the income expected to be earned by the subject property is estimated, allowing for reasonable expenses, vacancy, and collection loss, to arrive at net operating income (NOI). *Hometowne Assocs., L.P. v. Maley*, 839 N.E.2d 269, 275 (Ind. Tax Ct. 2005). The NOI is then converted to a present value by dividing it by a capitalization rate which

> generally reflects the annual rate of return necessary to attract investment capital and is influenced by such factors as "apparent risk, market attitudes toward future inflation, the prospective rates of return for alternative investments, the rates of return earned by comparable properties in the past, the supply of and demand for mortgage funds, and the availability of tax shelters."

*Id.* (citation omitted). In estimating the 2004 market value-in-use of the complex, Porter used Country Acres' 2003 gross rent of $633,222 as reported on its federal tax return to determine its annual gross income. (*See* Cert. Admin. R. at 82-83, 115-16.) Based on its 2003 profit and loss statement (P&L), Porter determined that Country Acres' "net income" was $185,543 (deducting $120,034 in actual repairs, but not real estate taxes). (*See* Cert. Admin. R. at 82-83, 276-79.) Porter then deducted $83,903 of replacement reserves (as ascertained through his reconciliation of market estimates and cost manual data) from the "net income" to arrive at a NOI of $101,640. (*See* Cert. Admin. R. at 83-84, 145-47, 279-85.) Porter applied a capitalization rate of 11.35% (as derived from Integra Realty Resources Inc.'s 2004 annual report and a 2.35% "real estate tax rider") to the NOI to arrive at a 2004 market value-in-use of $895,506. (*See* Cert. Admin. R. at 84-85, 127, 285-86, 292-94.) Porter then reduced that value by a 7% trending factor to arrive at a 1999 market value-in-use of $836,921. (*See* Cert. Admin. R. at 85, 128-30, 294-96.)

2005.[4]

In contrast, the Assessor presented a two-page analysis and the testimony of Mr. Joshua Petitt, another Indiana certified Level II assessor-appraiser. The Assessor's analysis (which also employed the income approach) established the market value-in-use of Country Acres' property at $2,393,000 on January 1, 1999. Petitt explained that the C&W appraisal supported the Assessor's analysis because, when trended back to January 1, 1999, it demonstrated that the property's market value-in-use was $2,135,900. (*See* Cert. Admin. R. at 249, 406-07.)

On January 21, 2009, the Indiana Board issued a final determination in which it reduced Country Acres' assessment to $2,135,900. The Indiana Board concluded that the C&W appraisal, with the application of a 7% trending factor, was the best evidence of the property's market value-in-use. (*See* Cert. Admin. R. at 39 ¶ 56, 43 ¶ 67.) In reaching this conclusion, the Indiana Board explained that Porter's analysis was unreliable because he was a contingent fee expert witness and his analysis accounted for the property's reserves twice and utilized an improper capitalization rate.[5] (*See* Cert. Admin. R. at 36-37 ¶¶ 46-49, 38-39 ¶ 54 (footnote added).)

On March 6, 2009, Country Acres initiated this original tax appeal. The Court

[4] In formulating that estimate, Sallander determined that, based on the market data and the subject's "historical" rental rates, Country Acres' potential gross income was $678,000. (*See* Cert. Admin. R. at 202-07.) She subsequently allowed for a 4% vacancy and collection loss, added other miscellaneous income, deducted operating expenses (including $25,000 in replacement reserves and $83,706 in real estate taxes), to arrive at a NOI of $149,324. (*See* Cert. Admin. R at 202, 208-11.) Sallander applied a capitalization rate of 6.75% (derived from two investor surveys) to the NOI and concluded that the complex was worth $2.2 million. (*See* Cert. Admin. R. at 212-13.)

[5] As to the Assessor's analysis, the Indiana Board explained it was unreliable because Petitt did not prepare it and "knew nothing" about the underlying data. (*See* Cert. Admin. R. at 39 ¶ 55.)

heard the parties' oral arguments on December 4, 2009. Additional facts will be supplied as necessary.

## STANDARD OF REVIEW

When this Court reviews a final determination of the Indiana Board, it is limited to determining whether it is:

> (1) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law;
>
> (2) contrary to constitutional right, power, privilege, or immunity;
>
> (3) in excess of statutory jurisdiction, authority, or limitations, or short of statutory jurisdiction, authority, or limitations;
>
> (4) without observance of procedure required by law; or
>
> (5) unsupported by substantial or reliable evidence.

IND. CODE ANN. § 33-26-6-6(e)(1)-(5) (West 2010). The party seeking to overturn an Indiana Board final determination bears the burden of demonstrating its invalidity. *Osolo Twp. Assessor v. Elkhart Maple Lane Assocs.*, 789 N.E.2d 109, 111 (Ind. Tax Ct. 2003).

## ANALYSIS AND OPINION

In its appeal to this Court, Country Acres claims that the Indiana Board abused its discretion for two main reasons when it concluded that the C&W appraisal best reflected the market value-in-use of its complex. Country Acres first asserts that the Indiana Board's "unrelenting" focus on Porter's contingent fee arrangement was inappropriate and, as a result, it failed to recognize that Porter's analysis prima facie established the market value-in-use of its complex. In the alternative, Country Acres asserts that the Indiana Board simply erred in assigning a final value to the complex.

The Court will address each of these claims in turn.

**I.**

Country Acres maintains that the Indiana Board overstepped its authority by linking the probative value of Porter's entire analysis to his contingent fee arrangement. (*See* Pet'r Br. at 6; Oral Argument Tr. at 5.) Country Acres complains that in so doing, the Indiana Board simply ignored the facts underlying Porter's analysis, failed to give those facts the proper weight, and just assumed his analysis was incorrect. (*See* Oral Argument Tr. at 5-6.) Country Acres' complaints, however, are misplaced.

Several years ago, this Court explained that "the contingent nature of an expert witness's fee *goes to the weight*, not the admissibility, of the expert's testimony." *See Wirth v. State Bd. of Tax Comm'rs*, 613 N.E.2d 874, 877 (Ind. Tax Ct. 1993) (emphasis added). As the finder of fact, the Indiana Board is responsible for weighing the evidence and judging the credibility of witnesses; this Court will not interfere with that function absent an abuse of discretion. *See, e.g., Stinson v. Trimas Fasteners, Inc.*, 923 N.E.2d 496, 498-99 (Ind. Tax Ct. 2010). Consequently, the Indiana Board did not abuse its discretion in considering Porter's contingent fee arrangement; rather, it simply fulfilled its duties in that it reviewed all of the evidence before it.

Country Acres also claims that it prima facie established that the market value-in-use of its complex was $836,921 for the 2004 tax year. According to Country Acres, the Indiana Board erred in assigning the greatest weight to the C&W appraisal because the record evidence does not support the Indiana Board's findings that: 1) Porter "double dipped" in formulating the replacement reserve estimate; and 2) Porter's use of an 11.35% capitalization rate was improper. (*See* Oral Argument Tr. at 6-12.)

**(a) Replacement reserve estimate**

A "replacement reserve" is "[a]n allowance in an annual operating statement for replacement of short-lived items that will not last for the remaining economic life of a property." (Cert. Admin. R. at 110 (citation omitted).) In other words, "[p]arts of a building that normally must be replaced before the building reaches the end of its economic life should have an annual expense charge as a reserve for replacement[.]" (Cert. Admin. R. at 110 (quoting INTERNATIONAL ASS'N OF ASSESSING OFFICERS, PROPERTY ASSESSMENT VALUATION, 217-18 (2nd ed. 1996)).)

Country Acres asserts that Porter's replacement reserve analysis more accurately reflected its replacement reserve expenses than the C&W appraisal because Porter's analysis was based on the exact methodology contained in an assessing treatise and did not simply "manipulate" and partition its operating expense data. (*See* Pet'r Br. at 7-8; Pet'r Reply Br. at 3.) Furthermore, Country Acres explains that any "double-dipping" between its reported repair expenses and Porter's replacement reserve estimate would have been minimal, given that the only possible duplicate expense was a $9,415 heating/cooling expense. (*See* Pet'r Reply Br. at 3; Oral Argument Tr. at 11-12.) The Court disagrees.

The propriety of Porter's replacement reserve estimate does not simply turn on whether he used an approved methodology in formulating the estimate. *See, e.g., O'Donnell v. Dep't of Local Gov't Fin.*, 854 N.E.2d 90, 94-95 (Ind. Tax Ct. 2006) (discounting the importance of methodology). Rather, the probative value of that estimate requires an examination of the facts underlying the analysis. The administrative record in this case reveals that over a year before the Indiana Board

hearing, Porter received an e-mail from Frank Kelly, one of the Assessor's representatives, expressing his concerns as to the reliability of Porter's replacement reserve estimate. More specifically, Kelly explained that because apartment complexes "typically . . . repair/replace reserve items [] without ever maintaining actual reserves[] additional deductions for replacement reserves on top of the actual repair expenses are unwarranted." (Cert. Admin. R. at 139.) Kelly also suggested that Porter could link Country Acres' reported repair expenses with the items that were actually repaired, comparing those results to his replacement reserve analysis to verify his estimate. (*See* Cert. Admin. R. at 139.) During the Indiana Board hearing, Petitt's testimony echoed that of Kelly's: apartment complexes routinely "expensed" monies that should have been allocated to replacement reserves as repairs. (*See* Cert. Admin. R. at 418-19.) Furthermore, the C&W appraisal stated that Country Acres "historically" engaged in the practice. (*See* Cert. Admin. R. at 210.) Finally, when Porter was questioned about the possibility of an overlap as to these expenses, he simply responded: "I am not an accountant. I would suggest that if they're called repairs that's because the monies were . . . spent on repairs and not on replacement[s]." (Cert. Admin. R. at 333.)

These facts suggest that Country Acres' repair expenses, as reported on its P&Ls, most likely included expenses that should have been categorized as reserves. The facts also demonstrate that Porter's analysis accounted for Country Acres' actual repair expenses in addition to a separate replacement reserve estimate. Conversely, the C&W appraisal divided Country Acre's reported repair expenses into three distinct categories, one of which was a replacement reserve. Thus, the reasonable inference is that Porter's analysis accounted for Country Acres' replacement reserves twice and the

C&W appraisal did not. This Court will not disturb the Indiana Board's resolution of an issue if a reasonable person could view the record in its entirety and find enough relevant evidence to support that determination. *See Amax Inc. v. State Bd. of Tax Comm'rs*, 552 N.E.2d 850, 852 (Ind. Tax Ct. 1990) (stating that substantial evidence "is more than a scintilla[; i]t means such relevant evidence as a reasonable mind might accept as adequate to support a conclusion"). Accordingly, the Indiana Board's finding that Porter "double-dipped" in formulating his replacement reserve estimate is affirmed.

**(b) The capitalization rate**

Next, Country Acres contends that contrary to the Indiana Board's finding, Porter's use of a national investor survey and a real estate tax rider to arrive at an 11.35% capitalization rate was proper. (*See* Oral Argument Tr. at 6-9.) Country Acres claims that the Indiana Board should have recognized that the C&W appraisal's capitalization rate of 6.75% was too low, given that the majority of the record evidence indicated that a 9% capitalization rate, at the very least, was much more appropriate. (*See* Oral Argument Tr. at 8-9.) Therefore, argues Country Acres, the Indiana Board's complete rejection of Porter's capitalization rate was an abuse of discretion. Again, the Court disagrees.

The valuation of property is the formulation of an opinion; it is not an exact science. When there are competing opinions as to how a property should be valued, the Indiana Board must determine which opinion is more probative. That determination is, essentially, the result of how effectively each party has persuaded the Indiana Board that its value opinion is more credible and reliable than that of the other. *See generally Trimas Fasteners*, 923 N.E.2d 496-502. Here, the Indiana Board found the C&W

appraisal to be more probative despite the fact that it used a lower capitalization rate and was prepared for the purposes of refinancing. (*See* Cert. Admin. R. at 41 ¶ 61 (explaining that the C&W appraisal was "more through" and "consistent" than Porter's analysis).) Based on its review of record evidence, the Court does not disagree. Consequently, the Indiana Board did not err in rejecting Porter's use of an 11.35% capitalization rate.

**II.**

Lastly, Country Acres maintains that the Indiana Board erred in reducing its assessment to $2,135,900 for the 2004 tax year. More specifically, Country Acres explains that because the Indiana Board determined that the application of a 7% trending factor to the C&W appraisal was proper, its final valuation should actually reflect the application of that trending factor. (*See* Oral Argument Tr. at 5, 13.) Country Acres explains that a review of the math demonstrates that only a 3% trending factor was applied to the C&W appraisal. (*See* Pet'r Br. at 12; Oral Argument Tr. at 5.) Country Acres is correct.

When a 7% trending factor is applied to the C&W appraisal, a final market value-in-use of $2,056,075 is established. Consequently, the Indiana Board erred when it determined that the market value-in-use of Country Acres' complex was $2,135,900 for the 2004 tax year.

**CONCLUSION**

For the above stated reasons, the Indiana Board's final determination with respect to Issue I is AFFIRMED. The Indiana Board's final determination with respect to Issue II, however, is REVERSED. The matter is REMANDED to the Indiana Board so

that it may instruct the appropriate assessing officials to assess the subject property consistent with this opinion.