

STATE OF MICHIGAN
DEPARTMENT OF LICENSING & REGULATORY AFFAIRS
MICHIGAN ADMINISTRATIVE HEARING SYSTEM
MICHIGAN TAX TRIBUNAL

TJM Hospitality LLC,
Petitioner,

v

MTT Docket No. 416195

City of Iron Mountain,
Respondent.

Tribunal Judge Presiding
Preeti P. Gadola

FINAL OPINION AND JUDGMENT

ORDER DENYING RESPONDENT'S MOTION TO DISMISS

INTRODUCTION

Petitioner, TJM Hospitality appeals the ad valorem property tax assessments levied by Respondent, City of Iron Mountain, against the real property owned by Petitioner for the 2011 tax year. The property under appeal is Parcel No. 22-051-701-911-00, a Days Inn, located in Iron Mountain, Michigan. Petitioner was represented by Juan Carbonell, and Respondent was represented by Robert Pirkola, attorney. Petitioner's witness was Tom Gilbert, appraiser, and Respondent's witnesses were Patty Roell, assessor, and Jim Schultheis, appraiser. The hearing of this matter occurred on August 20, 2013.

Respondent, City of Iron Mountain, assessed the property as follows:

Parcel Number: 22-051-701-911-00

Year	TCV	SEV	TV
2011	\$969,200	\$484,600	\$484,600

Respondent revised its contentions as follows:

Parcel Number: 22-051-701-911-00

Year	TCV	SEV	TV
2011	\$950,000	\$475,000	\$475,000

Petitioner's contentions of the property's True Cash Value ("TCV"), State Equalized Value ("SEV"), and Taxable Value (TV) are as follows:

Parcel Number: 22-051-701-911-00

Year	TCV	SEV	TV
2011	\$255,000	\$127,500	\$127,500

Based on the evidence, testimony, and case file, the Tribunal's independent determination of TCV, SEV, and TV of the subject properties for the years under appeal are as follows:

Parcel Number: 22-051-701-911-00

Year	TCV	SEV	TV
2011	\$494,700	\$247,350	\$247,350

PETITIONER'S CONTENTIONS

Petitioner contends that the subject property should be valued using the income approach. Petitioner presented an appraisal that indicates the appraiser considered each of the valuation approaches but determined that the only appropriate valuation approach for the subject property was the income approach. Petitioner contends that the occupancy rate for the subject ranges between 30 and

40 percent, which is typical of the market area. See Petitioner's Appraisal, p. 12.

The appraiser used Petitioner's actual income and expense report to derive his contention of true cash value at \$255,000.

PETITIONER'S ADMITTED EXHIBITS

P-1 Appraisal

P-2 Letter to Ms. Roell from Mr. Schultheis

PETITIONER'S WITNESS

Tom Gilbert

Tom Gilbert, Petitioner's expert witness, is a certified general appraiser.

Mr. Gilbert testified that he considered all three approaches to value and determined that "only the income approach would be, in this particular case, credible and reliable." Transcript at 15. He also stated that the motel business in the Upper Peninsula was down during the tax years at issue due to a decline in tourism and business travel as well as the overall economy. *Id.* at 16. He relied upon income statements for 2008, 2009, and 2010, to calculate his opinion of value under the income approach. These income statements were provided to Mr. Gilbert by Petitioner's representative. See Transcript at 18. Mr. Gilbert testified that he found these documents reliable, and the documents themselves indicate they were

prepared for Petitioner by its accountant. Transcript at 19-20. He utilized the *actual* income and expense information because he found it reasonable and to be the type of information a typical purchaser would rely upon. Transcript at 79-80. He testified that he normalized the income statements to “reflect a picture of the enterprise which the typical purchaser would accept as being what they can anticipate from the purchase of property.” Transcript at 72. This included the removal of amortization, depreciation, interest, and property taxes, revising the professional fee, and adding the expense of reserves. See Transcript at 53-56.

Mr. Gilbert testified that he adjusted the professional fee to \$5,000 because the appraisal is valuing the property for a typical buyer and seller. He stated that in his opinion, “the typical buyer would not be paying a parent corporation for this management. The management would be done in-house” Transcript at 42.

With regard to the reserve, he testified that:

[r]eserves is a figure that is taken to account for the accrued replacement costs every year of items that need to be replaced that are short-lived items. . . .It’s an expense that is occurring but not being realized at any given time. . . . Every year a prudent owner . . . would be setting aside a certain amount of money every year to replace the TV sets, and the floor coverings, and the furniture, and the bedding, and all these other items which are not going to live on the same life as the motel itself. Transcript at 56-57.

He also indicated that the \$30,000 figure was derived by considering approximately \$5,000 to \$7,000 per room spread over a 7 to 10 year timeframe. *Id.* at 58. Property tax was not used as an expense but was used to calculate the overall capitalization rate, based upon the current millage rate. Transcript at 60-61.

Mr. Gilbert testified further that the cost of personal property should be removed because the appraisal is of the real estate only. His value of 15 percent is for replacement cost and not depreciated cost as indicated in the assessment of personal property. See Transcript at 66. He also testified that a franchise fee would be an expense that a new purchaser would incur and that this cost ranges from \$30,000 to \$50,000. See Transcript at 68-69.

Mr. Gilbert stated that he used a banded rate of investment to develop his cap rate. He testified that he “looked at the financing that was available . . . at that time. And then [he] used a blend of what’s called a mortgage constant with the equity yield to come up with a cap rate.” Transcript at 77.

Mr. Gilbert also testified that he did not consider the purchase of the subject property in 2007 because it did not appear in his research. He stated that “per USPAP requirements, [he is] required to do a three-year search of the sales history. And beyond that, [he] would not normally search.” Transcript at 34. He further testified that a sale of the subject that is older than this three-year limitation is not

relevant and does not need to be considered. See *Id.* Further, his non-consideration of the purchase price is not failing to consider the sales comparison approach, because the sales comparison approach “revolves around the sale of competitive properties.” Transcript at 34.

RESPONDENT’S CONTENTIONS

Respondent contends that Petitioner, a corporation, cannot be represented at hearing by a non-attorney. More specifically, Respondent indicates that “corporations are not capable of being represented in a pro-per status.” Transcript at 9.

Respondent also contends that Petitioner failed to meet its burden of going forward with the evidence. Specifically, Respondent contends that under *Jones & Laughlin Steel Corp v City of Warren*, 193 Mich App 348; 483 NW2d 416 (1992), the Tribunal has the duty to render an independent determination of value and that *Meadowlanes Ltd Dividend Housing Ass’n v City of Holland*, 437 Mich 473; 473 NW2d 636 (1991) sets forth the three approaches to value, and it is the “Tribunal’s duty to determine which approaches provide the most accurate valuation under the individual circumstances of each case.” Transcript at 85-86. Respondent further contends that “the only evidence brought forward by the petitioner includes a sole reliance on the income approach. Thus, tying the Tribunal’s hand. . . .” *Id.* at 86.

Respondent, therefore, contends that the case “can be properly dismissed on the failure to meet the burden of going forward with the evidence” *Id.* at 87.

RESPONDENT’S ADMITTED EXHIBITS

R-1 Appraisal

RESPONDENT’S WITNESSES

Patty Roell

Patty Roell, assessor for the City of Iron Mountain, testified that she used land sale studies of commercial land to develop the land value of \$305,000. Transcript at 92. She also testified that she believed that the property was purchased in October 2006 for \$850,000. *Id.* Since then, she testified that “[t]hey tore down, I believe it was a home, and a drive-up part of the hotel, and then they added the pool and they added some more rooms and they added a canopy. I think that was in 2008.” Transcript at 93.

James Schultheis

James Schultheis, Respondent’s appraiser and valuation expert, testified that he determined that the property should be valued at \$950,000 including personal property and business fixtures. Transcript at 102. He testified that he also utilized the income approach. Mr. Schultheis testified that a potential buyer is purchasing a

business entity, including the personal equipment, thus he did not reduce his valuation for the cost of the personal property. Transcript at 102. He further indicated that he looked at the income and expense sheets submitted by Petitioner and found that the gross sales figures were reasonable and similar to a comparable motel. Transcript at 104. The income utilized was the average of Petitioner's income for 2009 and 2010 "which are the best two years." Transcript at 113.

However, Mr. Schultheis testified that he did not find Petitioner's expenses to be reasonable. "There [were] just too many gaping holes and professional fees, and depreciation not being there. . . . [I]t just looked strange to me, so I didn't feel like I had to use those." Transcript at 104-105. He further testified that expenses should run around 60 percent of gross income. However, he testified that he could not specifically identify the source of the information upon which he was relying. See Transcript at 110-111. He also indicated that this document was at least 10 years old but that he does not believe that the numbers have varied much over the years. Transcript at 140. He also stated that he does not know the hotels that were included and stated that he thinks the hotels used "are in the north central United States." *Id.* He further stated that he chose to be more conservative and use about 75 percent of expenses "because of the economy being slow and being in recessionary mode." Transcript at 112.

Mr. Schultheis also testified that the best way to get a cap rate is from the market but that was difficult because of the limited sales. He further stated that he got his cap rate from a report, but he was not “sure where it appeared but the last page [of the report] has the girl’s references and who she works for.” Transcript at 114. He further testified that he did not use the numbers in this article. The article indicates that the 18.5 percent equity rate for limited service motels, but he chose to use 12 percent because he has “seen that number locally” and stated that the rate in the article is “more for the large players, the people who make larger loans for larger investments.” Transcript at 120. He further stated that he does not know what data this article tracks specifically. Transcript at 140. He testified that he calculated the capitalization rate the same as Petitioner’s appraiser, other than adding in a property tax factor and a mortgage constant. See Transcript at 116.

Mr. Schultheis stated that he also used the sales comparison approach. He looked at four sales which are “somewhat dated.” Transcript at 122. He testified that in the Upper Peninsula there will always be limited sales and you must “use what you can.” Transcript at 123. The best sale was in 2000 for \$1,400,000. See Transcript at 125-126. There is also a comparable on the market listed for \$950,000, 46 rooms, and is about 15 to 16 years old. Transcript at 128-129. He further indicated that there were some sales between 2008 and 2010 but they were

foreclosure sales. He testified that these were not used because they were “more dated and don’t really relate to a nice unit like this.” Transcript at 154. He further testified that one of his comparables resold and commented “[w]ow, this is – this is December of 2010. I could have referenced it I guess.” Transcript at 156.

Mr. Schultheis testified that he performed the cost approach even though it is not widely used because of the difficulty of calculating depreciation. Transcript at 131. He stated that he used the Michigan Assessor’s Manual “even though they haven’t updated that since 2003” and that headed 11 percent as an inflation factor. Transcript at 132. He testified that this percentage is not in the Assessor’s Manual and that he actually thinks it may be too low. Transcript at 133.

FINDINGS OF FACT

1. The subject property is identified as Parcel No. 22-051-701-911-00 and is located at 2001 South Stephenson Avenue, Iron Mountain, Michigan.
2. The subject is classified as Commercial real property.
3. The subject property contains a 45 room motel, pool, exercise room, laundry facility and canopy.
4. During the tax year at issue, the subject was operated as a Days Inn.
5. Petitioner’s appraisal and contention of value of \$255,000 is based upon only the income approach to value, although the cost and sales comparison approaches were considered.

6. Respondent's appraisal and contention of value of \$950,000, includes personal property and business fixtures, is based upon a combination of the sales and income approaches. Respondent's appraiser indicated that the replacement cost was estimated at over 2 million but did not include this approach in the appraisal or rely upon this approach.
7. The most recent sale of the subject was in October 2007 for \$850,000; however, this sale included more acreage and other structures that are no longer present. This sale is *not* relevant to the valuation of the subject property as of December 31, 2010.

CONCLUSIONS OF LAW

The assessment of real and personal property in Michigan is governed by the constitutional standard that such property shall not be assessed in excess of 50% of its true cash value. See MCL 211.27a.

The legislature shall provide for the uniform general ad valorem taxation of real and tangible personal property not exempt by law except for taxes levied for school operating purposes. The legislature shall provide for the determination of true cash value of such property; the proportion of true cash value at which such property shall be uniformly assessed, which shall not . . . exceed 50 percent Const 1963, art 9, sec 3.

The Michigan Legislature has defined "true cash value" to mean:

. . . the usual selling price at the place where the property to which the term is applied is at the time of assessment, being the price that could be obtained for the property at private sale, and not at auction sale except as otherwise provided in this section, or at forced sale. MCL 211.27(1).

The Michigan Supreme Court has determined that “true cash value” is synonymous with “fair market value.” See *CAF Investment Co v State Tax Comm*, 392 Mich 442, 450; 221 NW2d 588 (1974).

Under MCL 205.737(1), the Tribunal must find a property's true cash value in determining a lawful property assessment. See *Alhi Dev Co v Orion Twp*, 110 Mich App 764, 767; 314 NW2d 479 (1981). The Tribunal is not bound to accept either of the parties' theories of valuation. See *Teledyne Continental Motors v Muskegon Twp*, 145 Mich App 749, 754; 378 NW2d 590 (1985). The Tribunal may accept one theory and reject the other, it may reject both theories, or it may utilize a combination of both in arriving at its determination. See *Meadowlanes Ltd Dividend Housing Ass’n v Holland*, 437 Mich 473, 485-486; 473 NW2d 636 (1991).

A proceeding before the Tax Tribunal is original, independent, and de novo. See MCL 205.735a(2). The Tribunal's factual findings must be supported by competent, material, and substantial evidence. See *Antisdale v Galesburg*, 420 Mich 265, 277; 362 NW2d 632 (1984); *Dow Chemical Co v Dep’t of Treasury*, 185 Mich App 458, 462-463; 462 NW2d 765 (1990). “Substantial evidence must be more than a scintilla of evidence, although it may be substantially less than a

preponderance of the evidence.” *Jones & Laughlin Steel Corp v City of Warren*, 193 Mich App 348, 352-353; 483 NW2d 416 (1992).

“The petitioner has the burden of proof in establishing the true cash value of the property.” MCL 205.737(3). “This burden encompasses two separate concepts: (1) the burden of persuasion, which does not shift during the course of the hearing; and (2) the burden of going forward with the evidence, which may shift to the opposing party.” *Jones & Laughlin, supra* at 354-355. However, “[t]he assessing agency has the burden of proof in establishing the ratio of the average level of assessments in relation to true cash values in the assessment district and the equalization factor that was uniformly applied in the assessment district for the year in question.” MCL 205.737(3).

The three most common approaches to valuation are the capitalization of income approach, the sales comparison, or market, approach, and the cost-less-depreciation approach. See *Meadowlanes, supra* at 484-485; *Pantlind Hotel Co v State Tax Comm*, 3 Mich App 170; 141 NW2d 699 (1966), *aff’d* 380 Mich 390 (1968). The market approach is the only appraisal method that directly reflects the balance of supply and demand for property in marketplace trading. See *Antisdale*. The Tribunal is under a duty to apply its own expertise to the facts of the case to determine the appropriate method of arriving at the true cash value of the property,

utilizing an approach that provides the most accurate valuation under the circumstances. See *Antisdale, supra* at 277.

At hearing in this matter, Respondent's representative indicated that a corporation cannot be represented by a non-attorney. However, TTR 223 clearly states that "[a]n attorney **or authorized representative** may appear on behalf of a party in a proceeding by signing the petition or other document initiating the participation of that party in the proceeding or by filing an appearance." [Emphasis added.] In addition, Respondent brought forth no case law supporting its position that a non-attorney cannot represent a corporation at the Michigan Tax Tribunal. The Tribunal finds, therefore, that Petitioner's authorized representative properly appeared on behalf of Petitioner in this case.

Respondent also made a Motion to Dismiss the case at hearing. Respondent contends that Petitioner failed to meet its burden of proof by failing to bring forth each of the three approaches to value. However, the Tribunal again notes that Respondent failed to present any case law that specifically indicates that to meet the burden of proof, specifically the burden of going forward with the evidence, that a petitioner must set forth each valuation approach. Rather, Respondent relies upon *Jones & Laughlin Steel Corp, supra*, to state that the Tribunal has the duty to render an independent determination of value, as well as, *Meadowlanes, supra*,

which set forth the three approaches to value and it is the “Tribunal’s duty to determine which approaches provide the most accurate valuation under the individual circumstances of each case.” Transcript, at. 85-86.

The case law cited by Respondent in favor of its Motion does not support Respondent’s position. The Tribunal finds that the burden of going forward with evidence requires that Petitioner set forth evidence of value. See *Jones & Laughlin Steel Corp, supra* at 355-356. Here, Petitioner did bring evidence of value, specifically its appraisal. The appraisal clearly states that all three approaches were considered but that the only reliable approach to value for the tax year at issue was the income approach. All three approaches are not, however, required to be considered. While *Meadowlanes, supra*, does set forth the three “traditional methods” it also indicates that “[v]ariations of these approaches and entirely new methods may be useful if found to be accurate and reasonably related to the fair market value of the subject property.” *Meadowlanes*, at 485. Thus, it is clear that there is no requirement that Petitioner must submit each of the three traditional approaches to value and Respondent’s Motion to Dismiss shall be denied.

Cost Approach

Both Respondent’s and Petitioner’s experts opined that the cost approach was not the most reliable method to value the subject property. Respondent’s

appraiser testified that the downfall of this approach is the difficulty of calculating depreciation. He also testified that he calculated the cost approach using the Michigan Assessor's Manual. Transcript at 133. Mr. Schultheis indicated that the cost manual has not been updated since 2003, which required him to apply an inflation adjustment factor. He stated that he utilized an 11 percent inflation factor and that this may be low. Transcript at 132-133. This 11 percent is not supported by any evidence or testimony on record. Using the Assessor's Manual and his inflation factor, Mr. Schultheis concluded a value of over \$2,000,000.

Respondent's appraisal at 6. The subject was also valued using the Assessor's Manual by Respondent's Assessor. The Assessor's valuation conclusion under this approach, using the same source, was \$969,200. These conclusions are drastically different from one another which demonstrate the unreliability of this approach with regard to the subject property.

Given the above, the Tribunal agrees with the expert opinions that the cost approach is not the most reliable valuation method for the subject property. The subject property was built in 1990 and had an addition constructed in 2007. Given the age of the subject, the cost approach is not as reliable as it is clear that the

subject is not a newly constructed property.¹ Further, “[t]he difficulty of estimating depreciation in older properties may diminish the reliability of the cost approach in valuing these properties.” The Appraisal Institute, *The Appraisal of Real Estate* (Chicago: The Appraisal Institute 13th ed. 2008) at 393. Thus, the Tribunal finds that the cost approach is not the best method of valuing the subject property for the tax year at issue.

Sales Comparison Approach

Petitioner’s appraiser considered the sales comparison approach but found that “[c]omparable sales are severely limited. A large portion of the available sales are viewed as being distress (REO properties) sales and are not utilized.”

Petitioner’s Appraisal at 12. Respondent’s appraiser, on the other hand, conducted a sales comparison approach utilizing four sales comparables.

Respondent’s Comparable No. 1 sold in December 2004, for \$2.1 million and is a 50 unit motel in Eagle River, Wisconsin. Respondent’s Comparable No. 2 sold in August of 2007 for \$2.08 million and is a 91 unit motel in Iron Mountain, Michigan. Respondent’s Comparable No. 3 sold in 2000 for \$1.04 million and is a 32 room motel in Gladstone, Michigan. Respondent’s Comparable No. 4 sold in

¹ See The Appraisal Institute, *The Appraisal of Real Estate* (Chicago: The Appraisal Institute 13th ed. 2008) at 382 (stating that “[t]he cost approach is most applicable in valuing new or proposed constructions when the improvements represent the highest and best use of the land and land value is well supported).

March of 2002 for \$830,000 and is a 50 room motel located in Menominee, Michigan. Each of these sales sold more than three years prior to the relevant valuation date of December 31, 2010. Thus, their reliability as indicators of market value as of that date is questionable.

Mr. Schultheis indicated that in his opinion the most comparable property was Comparable No. 3 which is a newer motel on the lower end of the value range. He also states that “[i]t is reasonable to assume that these comparable motel sales would have brought less money after the 2008.” Respondent’s appraisal at 8. This statement is not supported by any data or information to support that it would be lower. Mr. Schultheis continues in the narrative to state “[i]f the GIM dropped to the 2 to 3 x range it’s a 17% drop.” *Id.* This appears to be a hypothetical, and it is not clear how this relates to the subject’s value as of December 31, 2010.

Respondent’s appraiser also states that “[t]he subject’s current (2013) basic rate is ... \$65/night and its ADR is estimated to be closer to ... \$60 in 2010.” *Id.* Thus, he concludes that “it’s reasonable to expect the subject to sell at 2x gross in 2010 or \$920,000, less necessary repairs or room upgrades.” *Id.*

The Tribunal finds that Respondent has failed to support its contentions of value under the sales comparison approach. The sales evaluated in the appraisal all sold more than three years prior to the relevant date of sale and are not adjusted to

reflect a value as of the relevant tax day. These sales are not recent, and the Tribunal finds that they do not adequately reflect the market as of the relevant tax day.² Mr. Schultheis also *assumes* an average daily rate for the subject property in 2010 but provides no support or explanation for this assumption. In addition, Respondent's appraiser admittedly omitted a more recent sale of Comparable No. 2 from his appraisal. Regarding this sale, Mr. Schultheis stated at the hearing, "[w]ow, this is – this is December of 2010. I could have referenced it I guess." Transcript at 156. Thus, the Tribunal finds that Respondent's sales comparison approach is not credible and reliable evidence of value. It consists of dated sales and is based on assumptions and omits a relevant and more recent sale of a property that was considered comparable by Respondent's appraiser.

There is testimony from Respondent's assessor regarding the most recent sale of the subject property. Ms. Roell testified that she believed the property was purchased in October of 2006 for \$850,000. Transcript at 92. She also indicated that many changes have been made to the subject property including tearing down structures and adding new features. Petitioner's appraiser also testified regarding

² See *Tsvetanoff v Twp of Augusta*, unpublished opinion per curiam of the Court of Appeals, issued February 26, 2013 (Docket No. 309765) (holding that it was reasonable for the Tribunal to find Petitioner's sales unreliable evidence of value because they occurred more than one year prior to the relevant tax day and lacked appropriate market based adjustments; this holding was based upon the Court's decision in *Meadowlanes, supra*, that "[t]he sales-comparison approach indicates true cash value by analyzing *recent* sales of similar properties").

the sale. Mr. Gilbert specifically testified that the purchase of the subject did not appear in his research because the sale occurred more than three years prior to the relevant valuation date. He stated that per USPAP requirements and his expert opinion, a sale that is older than the three-year limitation is not relevant and does not need to be considered. See Transcript at 34. The Tribunal agrees and finds that the purchase of the subject in 2006 is not reflective of the market in 2010. In addition, the subject underwent several changes between the time of purchase and December 31, 2010, which also indicates that the purchase price is not a reliable indicator of value for the 2011 tax year.

Income Approach

The final value approach, which was submitted by both parties, is the income approach. Petitioner's appraiser and Respondent's appraiser utilized different figures to derive their very different valuation conclusions under this approach. Both appraisers started with income and expense reports provided by Petitioner for 2008, 2009, and 2010.

Respondent's appraiser found that the income portion of the reports was reasonable and reliable to utilize. He therefore relied upon these reports to average the 2009 and 2010 gross incomes (i.e., the two best years) to go forward with his income approach. See Transcript at 113. Mr. Schultheis also testified that he did

not find the expenses to be reliable. Transcript at 104-105. Rather, Mr. Schultheis found that the industry average for limited service hotels should run about 65 percent to 70 percent of the gross sales. To derive this range, he relied upon the chart provided in his appraisal, which indicates that a 64 Unit Franchise averages 60.2 percent expenses.³ See Respondent's Appraisal, Attachment entitled "Financial Guide." He found that this source which is, *allegedly*, a generalized average that he *believes* includes motels from Michigan is more reliable than Petitioner's statement which reflected actual expenses. See Transcript at 140. He testified specifically that, to him, Petitioner's expenses "just looked strange." Transcript at 105. Mr. Schultheis also testified that this document is at least 10 years old and he cannot specifically identify the source of this information. See Transcript at 110-111 and 140. Even if the Tribunal found this document reliable, Mr. Schultheis did not actually rely upon the numbers in the chart. He stated that for the subject it should range between 65 and 70 percent, but that he decided to use 75 percent to allow "for the depressed market and rather high fixed costs." Petitioner's Appraisal at 9.

³ The categories provided in the chart include: 64 unit franchise, 20 unit non-franchise, and 185 Motels No.Cent. U.S. The chart indicates that the 185 motels on average had 68.7 percent expenses while the 64 unit franchise had 60.2 percent.

The Tribunal finds that the chart utilized is not reliable. Mr. Schultheis is not sure what source this document comes from and has indicated that it is at least 10 years old. Thus, it is not clear how this “data” was calculated or what it truly represents. Thus, it is also not clear how the data is relevant to the expenses of a motel operating on December 31, 2010. As Mr. Schultheis cannot explain how the “average” expenses were calculated or derived, the additional percentage to account for the depressed market can also not be explained. Thus, Respondent’s determination of expenses is not supported by material and competent evidence on record and is not reliable.

Similarly, Mr. Schultheis testified that he relied upon the article attached to his appraisal to determine his cap rate of 10 percent. This article is entitled “Dramatic Decline in Hotel Capitalization Rates Reflects Shift in Market Sentiment” and is dated January 21, 2011. Respondent’s appraiser indicated that the subject is a limited service hotel. The article shows a cap rate of 6.7 percent based on historical net operating income (NOI) and a cap rate of 7.3 percent based on first year projected NOI. However, Mr. Schultheis utilized a cap rate of 10 percent. He indicated that the article used an 18.5 percent equity yield which he contends is “more for the large players, the people who make larger loans for larger investments” and that he thought locally this should be 12 percent.

Transcript at 120. Again, Respondent's appraiser did not cite any authority for this contention or provide any calculations or evidence to support this revision. Even if the Tribunal determines that the source is reliable and should be relied upon under TTR 255, Respondent's appraiser did not utilize the article to calculate the value of the subject property under the income approach and failed to establish that his revision to the cap rate is supported. As such, the Tribunal finds that the cap rate of 10 percent, as used by Respondent's appraiser, is not supported by competent, material, and substantial evidence.

Mr. Schultheis also testified that he did not extract the cost of personal property and fixtures from his valuation because the potential buyer would be purchasing a business entity, including the personal equipment, which should be included in the valuation. See Transcript at 102. However, the Tribunal finds that the valuation at hand, for tax assessment purposes, is of the real property only. Thus, the value of personal property and fixtures must be removed from the valuation. Hotels contain a significant investment in personal property consisting of furniture, fixtures, and equipment (or FF&E) that has a relatively short useful life and is subject to rapid depreciation and obsolescence. A hotel cannot accommodate guests and generate income without the provision of significant personal property and furnishings (i.e., the furnishings in the individual guest

rooms). This personal property is a material income producing factor of the enterprise. As a result, a portion of the overall income of the going concern is realized by the use of FF&E. As personal property in Michigan is taxed separately from real property and only the subject's real property is at issue here, the personal property's contribution to the income of the business enterprise and the value of the personal property at the subject must be isolated and excluded from the real property component of the subject. This is also supported by Petitioner's expert's testimony regarding the proper valuation method. Mr. Gilbert reliably testified that "since this [appraisal] is being done for the *assessment* of real property, then I have to get to real property." [Emphasis added.] Transcript at 64. The Tribunal agrees with Mr. Gilbert's expert opinion that the value of the personal property must be removed. Otherwise, the personal property value would be improperly taxed twice. Thus, the Tribunal finds that Respondent's valuation of the subject under the income approach inappropriately includes the value of the personal property which is separately assessed. Overall, Respondent's income approach is not a reliable indicator of true cash value.

As indicated above, Petitioner also provided an income approach. Unlike Respondent's appraiser, Petitioner's appraiser found both Petitioner's income and expense reports to be a reliable basis for calculating the value of the subject under

the income approach. Transcript at 19-20. Mr. Gilbert testified that he normalized the income and expenses and indicates in his appraisal that he removed the expenses for amortization, depreciation, interest, and property taxes. He reduced the professional fee to \$5,000 and added an expense of \$30,000 for reserve. The Tribunal agrees and finds that the actual income and expense reports, adjusted to “reflect a picture of the enterprise which the typical purchaser would accept as being what they can anticipate from the purchase of property” is more reliable than an industry average of expenses that is more than 10 years old. Transcript at 72. Petitioner’s appraiser’s testimony adequately supports both his adjustment for the professional fee and the expense for the reserve. With regard to the \$30,000 figure, Mr. Gilbert indicated that this was determined by using approximately \$5,000 to \$7,000 per room over a 7 to 10 year timeframe. Transcript at 56-57. This results in a range \$22,500 to \$31,500, and thus, Mr. Gilbert’s reserve amount is supported. Mr. Gilbert’s determination of net operating income is \$39,000, and is well supported on the record.

Mr. Gilbert utilized the banded rate of investment method to determine the capitalization rate. This is a reliable technique “in which the capitalization rates attributable to components of a capital investment are weighted and combined to derive a weighted-average rate attributable to the total investment.” The Appraisal

Institute, *The Appraisal of Real Estate* (Chicago: The Appraisal Institute 13th ed. 2008) at 505. Mr. Gilbert indicated that he “looked at the financing that was available . . . at that time. And then [he] used a blend of what’s called a mortgage constant with the equity yield to come up with a cap rate.” Transcript at 77. This methodology is supported and explained in *The Appraisal of Real Estate*. See The Appraisal Institute, *The Appraisal of Real Estate* (Chicago: The Appraisal Institute 13th ed. 2008) at 505-506. While Petitioner’s appraiser’s methodology is well supported by this source, Petitioner did not provide his work papers or any testimony demonstrating that he properly calculated the numbers. Mr. Gilbert’s capitalization rate was calculated utilizing numerous factors, and there is insufficient information on record to verify the accuracy or reliability of each facet. Thus, the Tribunal finds that Petitioner’s capitalization rate is not supported by substantial, competent, and material evidence on record.

As indicated above, only the subject’s real property is at issue here. Therefore, the value of the personal property at the subject must be isolated and excluded from the real property component of the subject. Petitioner’s appraiser properly concluded that the value of the personal property must be removed from the value of the subject. Mr. Gilbert indicated that he believed the value of the personal property was approximately 15 percent of the true cash value. He

indicated that he used replacement cost and reliably testified that the value deducted for personal property should be the replacement or contributory value rather than the depreciated value on the tax rolls. The Tribunal agrees. Mr. Gilbert also testified that the current assessment of \$83,000 was not surprising because that is the depreciated value of the personal property as reported by Petitioner. See Transcript at 66. The Tribunal finds that Mr. Gilbert's contention of 15 percent for replacement cost is supported based upon the assessed value of the personal property and Mr. Gilbert's expert opinion.

Given the above, the Tribunal finds that Petitioner's income approach requires modification to reflect the subject's true cash value as of December 31, 2010. The Tribunal finds that the only flaw of Petitioner's income approach is the lack of support for the capitalization rate.

The most reliable evidence of capitalization rate is actually found in Respondent's evidence. The article provided as an attachment to Respondent's appraisal is from HVS, a global consulting and research firm in the hospitality industry (i.e., hotels). Due to the lack of support for both Respondent's and Petitioner's capitalization rates, the generalized data in the article "Dramatic Decline in Hotel Capitalization Rates Reflects Shift in Market Sentiment" is the best source. Though the data used in this article is not specifically local to the

subject market, it is nevertheless the *best evidence* of capitalization rate on record.

The article specifically delineates capitalization rates for limited service hotels, such as the subject, and is dated January 21, 2011, just after the relevant tax day.

Thus, the Tribunal shall use the capitalization rate of 6.7 percent.⁴ Utilizing this cap rate, the Tribunal derives a rounded true cash value of \$582,000 (including personal property or FF&E). Removal of the personal property at 15 percent results in a final true cash value of \$494,700.⁵

Overall, the Tribunal finds that Respondent's appraisal is not a reliable indicator of value due to the lack of support for the adjustment and omission of calculations relating to the cost approach, the omission of more recent sales, and the lack of support for the expenses and cap rate used in the income approach.

When asked about his final valuation conclusion, Respondent's appraiser stated "[w]ell at [\$950,000] I'm at \$45 [per] square foot and I'm at \$21,000 [per] room. I think those are well discounted from replacement costs. I didn't want to go over a million dollars. . . . I like that two times gross income number." Transcript at 136.

This testimony does not support a reliable valuation conclusion. The Tribunal finds

⁴ Mellen, *Dramatic Decline in Hotel Capitalization Rates Reflects Shift in Market Sentiment*, HVS, January 21, 2011 <<http://www.hvs.com/article/5046/dramatic-decline-in-hotel-capitalization-rates-reflects/>> (Accessed June 14, 2011).

⁵ Using Mr. Gilbert's reliable NOI of \$39,000, the capitalization rate of 6.7 percent, and reducing that value by 15 percent for personal property.

that Respondent's appraisal is not reliable. Respondent also submitted the property record cards for the subject property containing the cost approach. The Tribunal has discussed above why, in this case, the cost approach is not the most reliable indicator of value. As such, the most reliable indicator of value on record is Petitioner's income approach, with the revisions discussed above. While Petitioner's income approach is not without flaws, it is, however, the best and most supported evidence of value on record. The Tribunal has revised Petitioner's income approach with regard to the capitalization rate and has reached an independent determination of true cash value of \$494,700.

As previously indicated, the Tribunal is under a duty to apply its own expertise to the facts of the case to determine the appropriate method of arriving at the true cash value of the property, utilizing an approach that provides the most accurate valuation under the circumstances. See *Antisdale, supra* at 277. In this case, the Tribunal has evaluated each of the three approaches and finds that the most reliable approach is the income approach. The Tribunal reviewed all evidence and testimony on record and made the independent determination that Petitioner's income approach, with modification, was the most appropriate method to value the subject property. Therefore, the Tribunal finds, based upon the Findings of Fact and the Conclusions of Law set forth herein, that the subject property is over-

assessed for the 2011 tax year. The subject property's TCV, SEV, and TV for the tax year(s) at issue are as stated in the Introduction section above.

JUDGMENT

IT IS ORDERED that Respondent's Motion to Dismiss is DENIED.

IT IS FURTHER ORDERED that the property's state equalized and taxable values for the tax year at issue are MODIFIED as set forth in the Introduction section of this Final Opinion and Judgment.

IT IS FURTHER ORDERED that the officer charged with maintaining the assessment rolls for the tax years at issue shall correct or cause the assessment rolls to be corrected to reflect the property's true cash and taxable values as finally shown in this Final Opinion and Judgment within 20 days of the entry of the Final Opinion and Judgment, subject to the processes of equalization. See MCL 205.755. To the extent that the final level of assessment for a given year has not yet been determined and published, the assessment rolls shall be corrected once the final level is published or becomes known.

IT IS FURTHER ORDERED that the officer charged with collecting or refunding the affected taxes shall collect taxes and any applicable interest or issue a refund as required by this Final Opinion and Judgment within 28 days of the entry of this Final Opinion and Judgment. If a refund is warranted, it shall include

a proportionate share of any property tax administration fees paid and penalty and interest paid on delinquent taxes. The refund shall also separately indicate the amount of the taxes, fees, penalties, and interest refunded. A sum determined by the Tribunal to have been unlawfully paid shall bear interest from the date of payment to the date of judgment, and the judgment shall bear interest to the date of payment. A sum determined by the Tribunal to have been underpaid shall not bear interest for any time period prior to 28 days after the issuance of the Tribunal's Final Opinion and Judgment. Pursuant to MCL 205.737, interest shall accrue (i) after December 31, 2009, at the rate of 1.23% for calendar year 2010, (ii) after December 31, 2010, at the rate of 1.12% for calendar year 2011, (iii) after December 31, 2011, and prior to July 1, 2012, at the rate of 1.09%, and (iv) after June 30, 2012, and prior to January 1, 2014, at the rate of 4.25%.

This Final Opinion and Judgment resolves all pending claims in this matter and closes this case.

By: Preeti P. Gadola

Entered: Nov 01, 2013