

TENNESSEE STATE BOARD OF EQUALIZATION
BEFORE THE ADMINISTRATIVE JUDGE

IN RE: **Directors Commons LLC**) **Shelby County**
Ward 060, Map 222, Parcel 00180)
)
Tax Year 2009) **Appeal No. 60211**

INITIAL DECISION AND ORDER

Statement of the Case

The subject property is presently valued as follows:

<u>LAND VALUE</u>	<u>IMPROVEMENT VALUE</u>	<u>TOTAL VALUE</u>	<u>ASSESSMENT</u>
\$588,000	\$1,031,300	\$1,619,300	\$647,720

An appeal has been filed on behalf of the property owner with the State Board of Equalization. The undersigned administrative judge conducted a hearing in this matter on February 29, 2012, in Memphis, Tennessee. The taxpayer was represented by Andrew H. Raines, Esq. The assessor of property was represented by John Zelinka, Esq.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

Subject property consists of a 10.607 acre parcel improved with eight buildings constructed in 1973 containing 131,426 square feet of flex warehouse space. The property is located at 3035 Directors Cove in Memphis, Tennessee. On the relevant assessment date of January 1, 2009, subject property had a vacancy rate of 67%.

The taxpayer contended that subject property should be valued at \$600,000. The taxpayer's sole witness was Eric Everett, the asset and property manager of subject property since 2006. Mr. Everett testified that he has worked in real estate for fifteen years and bought, sold and managed property during that time. Additionally, Mr. Everett stated that he worked as a

commercial real estate broker from 1997-2004 and has been a licensed general contractor since 2002.

Mr. Everett testified that in his opinion subject property is approaching the end of its useful life due to its physical condition. In support of this contention, he summarized a number of areas where the infrastructure was beginning to fail. Mr. Everett also testified concerning the deterioration of the area since FedEx relocated its offices and his lack of success finding tenants for the unoccupied space. Mr. Everett stated that in his opinion subject property experienced a decline in value of 50%-60% between mid-2007 and the relevant assessment date of January 1, 2009. Given all of the foregoing, Mr. Everett opined that subject property had a market value of \$600,000 on January 1, 2009.¹

The basis of valuation as stated in Tennessee Code Annotated § 67-5-601(a) is that “[t]he value of all property shall be ascertained from the evidence of its sound, intrinsic and immediate value, for purposes of sale between a willing seller and a willing buyer without consideration of speculative values. . .”

General appraisal principles require that the market, cost and income approaches to value be used whenever possible. Appraisal Institute, *The Appraisal of Real Estate* at 130 and 140-141. (13th ed. 2008). However, certain approaches to value may be more meaningful than others with respect to a specific type of property and such is noted in the correlation of value indicators to determine the final value estimate. The value indicators must be judged in three categories: (1) the amount and reliability of the data collected in each approach; (2) the inherent strengths and weaknesses of each approach; and (3) the relevance of each approach to the subject of the appraisal. *Id.* at 559-565.

¹ The taxpayer pre-filed an exhibit setting forth a contention of value of \$1,056,200 based upon the income approach. For whatever reason, the taxpayer did not rely on the exhibit at the hearing. Interestingly, if that income approach is modified by simply **increasing** what was presumably the effective tax rate from 1.44% to 2.72% and stabilizing the expenses at \$1.35 per sf, a value indication of \$1,341,086 results. As will be discussed below, that is virtually the exact value adopted by the administrative judge.

The value to be determined in the present case is market value. A generally accepted definition of market value for ad valorem tax purposes is that it is the most probable price expressed in terms of money that a property would bring if exposed for sale in the open market in an arm's length transaction between a willing seller and a willing buyer, both of whom are knowledgeable concerning all the uses to which it is adapted and for which it is capable of being used. *Id.* at 23.

In view of the definition of market value, the income-producing nature of the subject property and the age of subject property, generally accepted appraisal principles would indicate that the market and income approaches have greater relevance and should normally be given greater weight than the cost approach in the correlation of value indicators.

The assessor contended that subject property should be valued at \$1,619,300. In support of this position, the testimony and written analysis of Larry Cargile, TCA was offered into evidence. Mr. Cargile based his opinion of value on an income approach which assumed a market rental rate of \$6.00 per SF, a 50% vacancy and collection loss allowance, operating expenses (excluding taxes) of \$1.35 per SF and a loaded capitalization rate of 13.72%. Although Mr. Cargile's written analysis included several comparable sales, he relied strictly on the income approach in arriving at his estimate of value.

After having reviewed all the evidence in the case, the administrative judge finds that the subject property should be valued at \$1,341,100 based upon the following income approach:

Potential Gross Income	\$722,843
Less Vacancy & Collection Loss	<u>-361,422</u>
Effective Gross Income	\$361,421
Less Operating Expenses	<u>-177,425</u>
Net Operating Income (NOI)	\$183,996
NOI Capitalized @	<u>÷.1372</u>
Indicated Value Before Rounding	\$1,341,079
Adopted Value	\$1,341,100

As will be discussed below, the above income approach assumes a market rental rate of \$5.50 per SF, a vacancy and collection loss allowance of 50%, operating expenses of \$1.35 per SF, and a loaded capitalization rate of 13.72%.

Since the taxpayer is appealing from the determination of the Shelby County Board of Equalization, the burden of proof is on the taxpayer. See State Board of Equalization Rule 0600-1-11(1) and *Big Fork Mining Company v. Tennessee Water Quality Control Board*, 620 S.W.2d 515 (Tenn. App. 1981).

The administrative judge finds that Mr. Everett's experience as a property manager, commercial real estate broker and licensed general contractor make him competent to testify about matters within his areas of expertise affecting value such as the property's physical condition, leasing prospects etc. However, the administrative judge finds that he does not qualify as an expert in the valuation of property and is not competent to give an opinion of value. Moreover, even if Mr. Everett was competent to give such an opinion, his testimony was not supported with comparable sales or an income approach. The administrative judge finds that even bona fide experts must substantiate their opinions of value.

The administrative judge finds that Mr. Cargile's income approach should initially receive greatest weight, but Mr. Everett's testimony supports reducing the assumed market rental rate to \$5.50 per SF. The administrative judge finds that subject property is presently achieving an average rental rate of \$5.45 per SF and is unlikely to see any improvement in the near future due to both its high vacancy rate and the availability of competing space in the submarket.

The administrative judge finds that the taxpayer's limited proof concerning expenses supports Mr. Cargile's decision to utilize an expense allowance of \$1.35 per SF. In particular, the profit and loss statement entered into evidence as exhibit #2 indicates total actual expenses for 2008 of \$213,903. The administrative judge finds that the \$35,333 of property taxes have been

accounted for in the effective tax rate and must therefore be deducted from the expense total. Similarly, the administrative judge finds that the line item for business taxes of \$12,566 should be disallowed as well. See *805 Realty Corp. & Lebbes Realty* (Davidson County, Tax Year 2009) wherein the administrative judge disallowed a \$55,000 deduction for franchise and excise taxes ruling in relevant part as follows:

. . . operating expenses are normally those which pertain to the real estate and its management. Corporate taxes are expenses based upon the operation of a business and not inherent to the real estate. *See generally*, Appraisal Institute, *The Appraisal of Real Estate* at 484-490 (13th ed. 2008). Accordingly, the administrative judge finds that franchise and excise taxes do not constitute allowable operating expenses.

The income approach adopted by the administrative judge allows operating expenses of \$177,425. The taxpayer's actual operating expenses in 2008 were only \$166,004 excluding the taxes just discussed.

With respect to the capitalization rate, Mr. Cargile's analysis included survey information in support of his assumed base rate of 11%. Respectfully, Mr. Everett offered no sales or survey data in support of his testimony that a 12% rate was more appropriate. Accordingly, the administrative judge adopts Mr. Cargile's rate.

ORDER

It is therefore ORDERED that the following value and assessment be adopted for tax year 2009:

<u>LAND VALUE</u>	<u>IMPROVEMENT VALUE</u>	<u>TOTAL VALUE</u>	<u>ASSESSMENT</u>
\$588,000	\$753,100	\$1,341,100	\$536,440

Pursuant to the Uniform Administrative Procedures Act, Tenn. Code Ann. §§ 4-5-301—325, Tenn. Code Ann. § 67-5-1501, and the Rules of Contested Case Procedure of the State Board of Equalization, the parties are advised of the following remedies:

1. A party may appeal this decision and order to the Assessment Appeals Commission pursuant to Tenn. Code Ann. § 67-5-1501 and Rule 0600-1-.12 of the Contested Case Procedures of the State Board of Equalization. Tennessee Code Annotated § 67-5-1501(c) provides that an appeal **“must be filed within thirty (30) days from the date the initial decision is sent.”** Rule 0600-1-.12 of the Contested Case Procedures of the State Board of Equalization provides that the appeal be filed with the Executive Secretary of the State Board and that the appeal **“identify the allegedly erroneous finding(s) of fact and/or conclusion(s) of law in the initial order”**; or
2. A party may petition for reconsideration of this decision and order pursuant to Tenn. Code Ann. § 4-5-317 within fifteen (15) days of the entry of the order. The petition for reconsideration must state the specific grounds upon which relief is requested. The filing of a petition for reconsideration is not a prerequisite for seeking administrative or judicial review.

This order does not become final until an official certificate is issued by the Assessment Appeals Commission. Official certificates are normally issued seventy-five (75) days after the entry of the initial decision and order if no party has appealed.

ENTERED this 9th day of March 2012.



MARK J. MINSKY, Administrative Judge
Tennessee Department of State
Administrative Procedures Division
James K. Polk Building
505 Deaderick Street, Suite 1700
Nashville, Tennessee 37243-1402

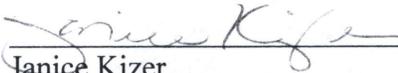
CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and exact copy of the foregoing Order has been mailed or otherwise transmitted to:

Andrew H. Raines, Esq.
Evans Petree PC
1000 Ridgeway Loop, Suite 200
Memphis, Tennessee 38120

Tameaka Stanton-Riley
Shelby Co. Property Assessor's Office
Appeals Department
1075 Mullins Station Road
Memphis, Tennessee 38134

This the 9th day of March 2012.



Janice Kizer
Tennessee Department of State
Administrative Procedures Division