REPRESENTATIVES FOR PETITIONER:
James W. Beatty, J.F. Beatty, and Jessica Findley, Landman & Beatty

REPRESENTATIVE FOR RESPONDENT:
Marilyn Meighen, Meighen & Associates, PC

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# BEFORE THE
# INDIANA BOARD OF TAX REVIEW

| | | |
|---|---|---|
| DAVIS-GRATNER, LLC | ) | Appeal from the Henry |
| | ) | County Property Tax Assessment |
| Petitioner, | ) | Board of Appeals |
| | ) | |
| v. | ) | Pet. Nos. 33-016-06-1-4-00015 |
| | ) | 33-016-06-1-4-00015a |
| HENRY COUNTY ASSESSOR | ) | 33-016-07-1-4-00002 |
| | ) | |
| Respondent. | ) | |
| | ) | Parcel Nos. 0308291400 |
| | ) | 0308291300 |
| | ) | |
| | ) | |
| | ) | Assessment Years: 2006 and 2007 |

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Appeal from the Final Determination of the
Henry County Property Tax Assessment Board of Appeals

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**January 13, 2010**

## FINAL DETERMINATION

The Indiana Board of Tax Review ("Board") having reviewed the facts and evidence, and having considered the issues, now finds and concludes the following:

## FINDINGS OF FACT AND CONCLUSIONS OF LAW

### INTRODUCTION

1. In these assessment appeals, the parties fiercely contested the subject property's 2006-2007 assessments and the closely related issue of whether store sales of Davis-Gratner's tenant were relevant to those assessments. But the case boils down to weighing the valuation opinions of the parties' various experts. In the end, the Board was persuaded by the opinion of Jay Allardt, the appraiser with the most experience in valuing fast-food restaurants and other commercial properties.

### PROCEDURAL HISTORY

2. Although these appeals involve a single property located at 1595 S. Memorial Drive in New Castle, the property was listed as two separate tax parcels for the March 1, 2006, assessment date. The parcels were later combined for the March 1, 2007, assessment.

3. Davis-Gratner filed Form 130 petitions challenging the subject property's 2006 and 2007 assessments. On December 20, 2007, and July 30, 2008, the Henry County Property Tax Assessment Board of Appeals ("PTABOA") issued Form 115 notices setting forth assessments with which Davis-Gratner disagreed. Davis-Gratner responded by filing Form 131 petitions with the Board on January 28, 2008, and August 13, 2008.

4. The Board scheduled a hearing on Davis-Gratner's appeals for March 11, 2009. Nine days before that hearing, at the Assessor's request, Commissioner Terry G. Duga issued subpoenas duces tecum to Marsha and David Gratner. Those subpoenas ordered the Gratners to appear at the hearing and to bring the following documents: "A copy of detailed store sales and expenses for 2004, 2005, and 2006 for the property commonly known as the New Castle Kentucky Fried Chicken located at 1595 South Memorial Drive, New Castle, Indiana." *Motion to Quash, Exs. 2-3.* The PTABOA had actually ordered Davis-Gratner to produce similar documents as part of the proceedings below, but Davis-Gratner had refused on grounds that those documents were irrelevant.

*Assessor's Designation of Evidence, Ex. 1(filed in conjunction with the Assessor's response to Davis-Gratner's Motion to Quash)*.

5. Because Davis-Gratner's counsel had not realized that the subpoenas required the Gratners to produce documents, the Gratners did not bring the subpoenaed documents to the Board's hearing. After conferring with counsel for both sides, the Board's designated administrative law judges, David Pardo and Jennifer Bippus, continued the hearing. The Board later rescheduled the hearing for July 27, 2009.

6. In the interim, Davis-Gratner filed a motion to quash the subpoenas and a motion for partial summary judgment. In both motions, Davis-Gratner argued that the subpoenaed documents were irrelevant because they related to the enterprise value of its tenant, Davis Gratner Restaurant Services, LLC, rather than to the value of the real estate itself. The Board denied Davis-Gratner's motions and ordered the Gratners to produce the subpoenaed documents at the re-scheduled hearing.

7. The ALJs conducted the hearing as scheduled on July 27 – 28, 2009. The following people appeared at the hearing and testified under oath[1]:

For Davis-Gratner:

Sheila J. Murray, Landman & Beatty
Marsha Gratner, Davis Gratner Restaurant Services, LLC
Jay E. Allardt, Indiana Certified General Appraiser
Daniel L. Semler, Indiana Certified General Appraiser
Judith Bunner, former Henry Township Assessor
Penny York, former Henry Township Assessor

For the Assessor:

Jodie Brown, Henry County Assessor[2]
Jeff Wuensch, Nexus Group

[1] The following people appeared at the hearing but did not testify: Bradley A. Berkemeier, David Gratner, and Thomas Cameron.
[2] Davis-Gratner actually called Ms. Brown as a witness in its case-in-chief.

James A. Cecil, Indiana Certified Residential Appraiser

8. Davis-Gratner offered the following exhibits[3]:

| | |
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| Petitioner's Exhibit 1: | 2006 Notice of Assessment – Form 11; PRC for 1300 |
| Petitioner's Exhibit 1A: | 2006 Notice of Assessment – Form 11; PRC for 1400; Photo 978 S. Memorial Dr. |
| Petitioner's Exhibit 1B: | PRC Razzle's Bar; 2 Photos – 950 S. Memorial Dr. |
| Petitioner's Exhibit 1C: | PRC Lida's in old Pizza Hut; Photo – 1008 S. Memorial Dr. |
| Petitioner's Exhibit 1D: | PRC Stack's; Photo 1552 S. Memorial Dr. |
| Petitioner's Exhibit 1E: | PRC Taco Bell; Photo – 990 S. Memorial Dr. |
| Petitioner's Exhibit 1F: | PRC McDonald's; Photo – 1088 S. Memorial Dr. |
| Petitioner's Exhibit 1G: | PRC Myers; Photo – 1488, 1502, 1532 S. Memorial Dr. |
| Petitioner's Exhibit 1H: | PRC Subway; Photo – 1038 S. Memorial Dr. |
| Petitioner's Exhibit 1I: | PRC Lee's Famous Recipe; Photo – 341 Trojan Ln.; Google of same address; |
| Petitioner's Exhibit 1J: | KFC Neighborhood Area Comparison from 2005-06; |
| Petitioner's Exhibit 1K: | Photos of Fast Food from Real Property Assessment Guideline |
| Petitioner's Exhibit 1L: | Photos of Fast Food from Real Property Assessment Guideline |
| Petitioner's Exhibit 1M: | KFC Neighborhood Area Comparison from 2005-06 on square footage basis |
| Petitioner's Exhibit 2: | 2008 Notice of Assessment - Form 11 C/I; PRC for Davis Gratner Kentucky Fried (old & new); Photo - 978 S. Memorial Dr. |
| Petitioner's Exhibit 2A: | PRC – Razzles Bar; Photo of sign & building |
| Petitioner's Exhibit 2B: | PRC – Lida's in old Pizza Hut; Photo of 1008 S. Memorial Dr. |
| Petitioner's Exhibit 2C: | PRC – Stacks |
| Petitioner's Exhibit 2D: | PRC – Vacant Taco Bell; Photo – 990 S. Memorial Dr. |
| Petitioner's Exhibit 2E: | PRC – McDonalds; Photo – 1088 S. Memorial Dr. |
| Petitioner's Exhibit 2F: | PRC – Myers; Photo 1552, 1488, 1502, 1532 S. Memorial Dr. |
| Petitioner's Exhibit 2G: | PRC Subway; Photo – 1038 S. Memorial Dr. |
| Petitioner's Exhibit 2H: | Lees Famous Recipe; photo 341 Trojan Ln. |
| Petitioner's Exhibit 2I: | 4/25/08 letter from Henry Township Assessor |
| Petitioner's Exhibit 2J: | KFC Neighborhood Area Comparison 2006-07 |

[3] Petitioner's exhibits 1J and 17 were admitted over the Assessor's objections. Petitioner's exhibits 1M and 2M were admitted over objection but then withdrawn. Although Davis Gratner identified a Petitioner's exhibit 4 in its exhibit list, Davis-Gratner did not offer that exhibit. Davis-Gratner similarly did not offer any exhibits numbered 11, 14 or 15.

| | |
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| Petitioner's Exhibit 2K: | Photos of Fast Food from Real Property Assessment Guideline |
| Petitioner's Exhibit 2L: | Photos of Fast Food from Real Property Assessment Guideline |
| Petitioner's Exhibit 3: | Henry County PTABOA order for the Production of Documents |
| Petitioner's Exhibit 3A: | Assessors Response to Petitioner's Request for Admissions and First Set of Interrogatories |
| Petitioner's Exhibit 3B: | Deposition of Jodie Brown and all exhibits made part of the deposition |
| Petitioner's Exhibit 4A: | Henry County: 2006 Annual Trending Overview of State Road 3/Memorial Dr. Land Values, Market Areas, Values, Influence Factors & Notes |
| Petitioner's Exhibit 4B: | Map of 1595 S. Memorial Dr. |
| Petitioner's Exhibit 4C: | Photos and Property Record Cards – 1704 S. Scatterfield Rd., Anderson, IN; PRC KFC of Madison County; Photo – 400 E. 5th St., Connersville; PRC KFC Connersville; Photo of KFC; PRC 309 W. Washington, Crawfordsville; Photo of 1801 W. McGalliard Rd., Muncie, PRC 801 W. McGalliard Rd., Muncie, Photo – 2324 S. Madison St., Muncie; PRC 2324 S. Madison St. |
| Petitioner's Exhibit 4D: | KFC Franchise Comparison 2006/2007 |
| Petitioner's Exhibit 5: | Appraisal prepared by Dan Semler |
| Petitioner's Exhibit 5A: | Appraisal Opinion Letter prepared by Dan Semler |
| Petitioner's Exhibit 6: | Form 8825 Rental Real Estate Income and Expenses of a Partnership or an S Corp./Davis Gratner LLC – 2005; Form 1120 S – Tax Return 2005/Davis Gratner |
| Petitioner's Exhibit 7: | Form 8825 Rental Real Estate Income and Expenses of a Partnership or an S Corp./Davis Gratner LLC – 2006; Form 1120 S – Tax Return 2006/Davis Gratner |
| Petitioner's Exhibit 8: | Davis/Gratner Lease Agreement |
| Petitioner's Exhibit 9: | Davis/Gratner Corporate Documents |
| Petitioner's Exhibit 10: | Jay Allardt Curriculum Vitae |
| Petitioner's Exhibit 12: | Square footage comparison of Cecil appraisal sales data and actual assessments |
| Petitioner's Exhibit 12A: | Arby's Connersville – Sales Disclosure and Property Record Cards |
| Petitioner's Exhibit 12B: | Arby's Muncie – Sales Disclosure and Property Record Cards |
| Petitioner's Exhibit 12C: | Fazolis Muncie – Sales Disclosure and Property Record Cards |
| Petitioner's Exhibit 12D: | Taco Bell Anderson – Sales Disclosure and Property Record Cards |
| Petitioner's Exhibit 12E: | Wendy's Anderson – Sales Disclosure and Property Record Cards |

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| Petitioner's Exhibit 12F: | Taco Bell Connersville – Sales Disclosure and Property Record Cards |
| Petitioner's Exhibit 12G: | Perkins Anderson – Sales Disclosure and Property Record Cards |
| Petitioner's Exhibit 12H: | New Castle Subway Agent Sales Report and Sales Disclosure |
| Petitioner's Exhibit 12I: | Logansport KFC Agent Sales Report |
| Petitioner's Exhibit 12J: | CNL Income Fund Memorandum of Lease |
| Petitioner's Exhibit 12K: | Realty Income Corporation Memorandum of lease |
| Petitioner's Exhibit 13: | Copy of *Hurricane Food, Inc. v. White River Twp. Assessor*, 836 N.E.2d 1069 (Ind. Tax Ct. 2005) |
| Petitioner's Exhibit 16: | Demonstrative exhibit depicting subject property neighborhood comparison properties |
| Petitioner's Exhibit 17: | Information from Marshall Valuation Service (8 pages) |

9. The Assessor offered the following exhibits[4]:

Respondent's Exhibit 1: Property Record Cards for:

(a) Davis Gratner Kentucky Fried Chicken Restaurant (parcel ending in 291300)
(b) Davis Gratner Kentucky Fried Chicken (parcel ending in 291400)
(c) Maple Properties, LLC
(d) RIC Properties, LTD
(e) Realty Income, Corp
(f) RIC Properties, LTD
(g) Franchise Realty Corp.
(h) McDonald's Corp
(i) Vincent Realty 200, LLC
(j) New Castle SB, LLC
(k) George R. Reilly
(l) Dellac, Inc.
(m) Fort Shirk Properties, LLC
(n) Develescope LLC
(o) First Fiscal Fund Co. et.al.
(p) Steak n Shake Operators, Inc.
(q) Green Investments, LLC
(r) BEF REIT, Inc.
(s) CNL Restaurant Invest II
(t) Sun Ace Retail, LLC 2.09%
(u) Green Investments, LLC
(v) Green Investments, LLC

[4] Respondent's exhibits 15-17 and 19 were admitted over Davis-Gratner's objections.

| | |
|---|---|
| Respondent's Exhibit 2: | Property Record Cards and Sales Disclosure Forms for:<br>(a) O'Reilly Automotive, Inc.<br>(b) Maple Properties, Inc.<br>(c) McDonald's Corp.<br>(d) New Castle SB, LLC<br>(e) Dellac, Inc.<br>(f) Fort Shink Properties, LLC<br>(g) Develescope, LLC<br>(h) Steak N Shake Operations, Inc. (includes closing statement) |
| Respondent's Exhibit 3: | Commercial Land on State Road 3/Memorial Drive |
| Respondent's Exhibit 4: | Lease Agreement between Develescope, LLC and White Castle Indiana, LLC |
| Respondent's Exhibit 5: | Ground Lease between Pizza Hut of America and Douglas Furbee |
| Respondent's Exhibit 6: | State-Wide Fastfood Restaurant Sales Spreadsheets with supporting documents |
| Respondent's Exhibit 7: | LoopNet listing for:<br>(a) Arby's/Dubois County<br>(b) Steak n' Shake/Lawrence County<br>(c) Steak n' Shake/Marion County |
| Respondent's Exhibit 8: | *The Valuation of Fast Food Restaurants*, IAAO Volume 2, Number 5, September/October 2004 |
| Respondent's Exhibit 9: | January 4, 2008, letter from DLGF to Henry County Assessor; October 26, 2006, letter from DLGF to Henry County Assessor |
| Respondent's Exhibit 10: | Appraisal by James A. Cecil of Hoosier Appraisal Service, Inc. |
| Respondent's Exhibit 11: | Property Record Cards and Sales Disclosure forms (or computer information) for:<br>(a) Cole MP MUY Portfolio II, LLC<br>(b) Net Lease Funding 2005, LP<br>(c) GLS Associates, LLC<br>(d) GE Capital Franchie Finance Corp<br>(e) Hong Fong<br>(f) Net Lease Funding 2005, LP<br>(g) Realty Income Corporation |
| Respondent's Exhibit 12: | Letter dated November 1, 2008, from James A. Cecil to Jeff Wuensch |
| Respondent's Exhibit 13: | Henry County PTABOA Order for Production of Documents with letter dated October 10, 2007, from Marsha Gratner to Henry County Assessor and proofs of mailing |
| Respondent's Exhibit 14: | *Conner et. al. v. McDaniel et. al.* (Ind. Ct. App. March 6, 2009) |

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| Respondent's Exhibit 15: | KFC Restaurant Services, LLC Profit & Loss Detail June 2004 through May 2005 |
| Respondent's Exhibit 16: | KFC Restaurant Services, LLC Profit & Loss Detail June 2005 through May 2006 |
| Respondent's Exhibit 17: | KFC Restaurant Services, LLC Profit & Loss Detail June 2006 through May 2007 |
| Respondent's Exhibit 18: | Henry County GIS Map (demonstrative) |
| Respondent's Exhibit 19: | Income-approach calculations prepared by Jeff Wuensch |
| Respondent's Exhibit A: | Fax coversheet from Marilyn Meighen to Jim Beatty and J.F. Beatty and subpoenas duces tecum for Marsha and David Gratner (offered at March 11, 2009, hearing) |

10. The Board recognizes the following items as part of the record of proceedings and labels them as Board Exhibits:

    Board Exhibit 1 – The Form 131 petitions
    Board Exhibit 2 – Hearing sign-in sheets from July 27-28, 2009, and March 11, 2009, hearings

    In addition, the Board incorporates into the record all filings by the parties and all orders and notices issued by the Board or its duly authorized administrative law judges, including all hearing notices and the Board's July 9, 2009, Order Granting, in Part, Petitioner's Motion to Strike and Denying Petitioner's Motion to Quash and Motion for Partial Summary Judgment.

11. The Form 131 petitions for Davis-Gratners' appeal of the subject property's March 1, 2006, assessment created some confusion about the property's assessed value of record. At the hearing, the parties stipulated that the property was assessed for a total of $619,600, broken down as follows:

    <u>Parcel 0308291300</u>

    Land: $169,000 Improvements: $16,200

    <u>Parcel 0308291400</u>

    Land: $171,000 Improvements: $263,400

12. For March 1, 2007, the subject property was assessed as follows:

    Land: 505,000 Improvements: $389,500 Total: $894,500

13. Davis-Gratner requested alternative values derived from the opinions of its two appraisers. Based on Daniel Semler's opinion, Davis-Gratner asked for an assessment of $335,000 for each year. Barring that, Davis-Gratner asked for assessments matching Jay Allardt's valuation opinion—$480,000 for 2006 and $487,200 for 2007. *Petitioner's Post-Trial Brief at 17*.

## FINDINGS OF FACT

### A. The Subject Property

14. The subject property consists of approximately 1.51 acres of land containing a 3,558-square-foot restaurant building, a 960 square-foot garage or utility building, and site improvements such as paving and fencing. *Resp't Ex. 1; see also, Pet'r Ex. 5 at 7-8; Resp't Ex. 10 at 20*.

15. The property is located along South Memorial Drive, which is New Castle's primary commercial strip. *See, e.g., Resp't Ex. 1; Semler testimony, Cecil testimony*. The main building houses a Kentucky Fried Chicken ("KFC") franchise restaurant. The building was constructed in 1967, although it has been updated through the years. *Pet'r Ex. 5 at 3*. The building was remodeled in 2004, but neither party offered evidence to describe what that remodeling entailed other than that KFC required upgrades as part of its franchise agreement. *See M. Gratner testimony*.

16. Originally, the subject property and the KFC franchise that occupied it were both owned by the same entity—Davis-Gratner Kentucky Fried Chicken Restaurant, Inc. *M. Gratner testimony; Pet'r Ex. 9*. In June 2004, however, that corporation apparently transferred its assets to two new entities—Davis-Gratner, LLC, which now owns the subject property, and Davis Gratner Restaurant Services, LLC ("Restaurant Services"), which owns and

operates the KFC franchise.[5] *See id*. The same two principals—David Gratner and his 84-year-old aunt, Joan Davis—own both entities. Although those two entities apparently began operating in June 2004, they did not file organizational documents with the Indiana Secretary of State until December 13, 2006. *Id*. Marsha Gratner, David's wife and an employee of Restaurant Services who does the books for Davis-Gratner, testified that the gap stemmed from a misunderstanding with the entities' attorney about who was supposed to file those documents. *M. Gratner testimony*. In any event, the principals apparently still treated the original corporation as continuing to have some interest in the property, given that, on the Form 130 petitions, David Gratner identified the property owner as "Davis-Gratner KFC Restaurant, Inc." *Board Ex. A*. The Form 131 petitions list the same owner, but add "a/k/a Davis Gratner LLC." *Id*.

17. In any event, on June 1, 2004, Davis-Gratner and Restaurant Services entered into a 10-year lease. Under that lease, Davis-Gratner was responsible for paying real estate taxes and insuring the building while Restaurant Services paid utilities. *Pet'r Ex. 8*. Although the lease called for annual rent of $49,200 payable in monthly installments of $4,100, Restaurant Services often paid different amounts. *M. Gratner testimony; Resp't Exs. 15-17*. From June 1, 2004, to May 31, 2005, Restaurant Services paid $ in rent. That dropped to $ for 2005-2006, and then increased to $ for 2006-2007. *M. Gratner testimony; Resp't Exs. 15-17*. The amount fluctuated for various reasons, including an increase in property taxes and Davis-Gratner's need to repay a loan from Joan Davis and Marsha Gratner for the 2004 remodeling project. *M. Gratner testimony*.

**B. Commercial property assessments in Henry County**

18. Indeed, Davis-Gratner's property taxes increased dramatically beginning with the 2006 assessment year. In 2005, the subject property was assessed for a total of $249,400.

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[5] Davis-Gratner's post-hearing brief refers to the franchise owner as "KFC Restaurant Services, Inc." *Petitioner's Post-Trial Brief at 3*. The "Profit & Loss Detail" reports produced by the Gratners in response to the subpoenas duces tecum refer to "KFC Restaurant Services, LLC." *See Resp't Exs. 15-17*. It is unclear whether those are alternate names for Davis Gratner Restaurant Services, LLC or instead refer to independent entities that have some ownership interest in the restaurant.

*Resp't Ex. 1*. That jumped to $619,600 for 2006 and to $894,500 for 2007. *Id.; see also oral stipulation regarding 2006 assessment*. Those increases led to Davis-Gratner's appeals.

19. Jeff Wuensch, the co-owner of Nexus Group, a consulting firm hired by Henry County in 2002, explained the changes in those assessments. In preparing for 2006—the first year of annual adjustments[6]—Nexus became concerned that commercial properties along Memorial Drive had been undervalued in the 2002 general reassessment and that commercial properties outside that area had been overvalued. *Wuensch testimony; see also, Resp't Ex. 2 (showing 2002-2005 assessments for properties along Memorial Drive and sale prices from 2004-2005).* Nexus therefore re-examined neighborhood delineations and further stratified those neighborhoods into market areas. Nexus used a variety of sources to determine new land values. *Wuensch testimony*. For example, Nexus looked at sales and at ground leases for the Pizza Hut and White Castle restaurants on Memorial Drive. *Id.; Resp't Exs. 4-5.* Because Nexus did not have any employees who lived in New Castle, it also consulted with Daniel Semler, a local appraiser who testified for Davis-Gratner in this case. In addition, Nexus took at least three steps to address improvement values:

- It visited commercial properties to update information about the physical characteristics of the improvements located on those properties;
- It evaluated sales and income data to make value adjustments; and
- It used information from the United States Bureau of Labor Statistics to create an index from which it updated the cost tables set forth in the Real Property Assessment Guidelines for 2002 – Version A.

*Wuensch testimony*.

[6] *See* Ind. Code § 6-1.1-4-4.5 (requiring the Department of Local Government Finance to adopt rules for annually adjusting assessments beginning with the 2006 assessment date).

20. Those efforts culminated in annual adjustments that significantly increased the assessments for many, if not all, commercial properties on the prime strip along Memorial Drive. *See id*.

21. Following Davis-Gratner's appeal of the subject property's 2006 assessment, the Assessor became concerned that the assessments of fast-food restaurants might not have been uniform. So Nexus inspected those properties for the second time in two years, looking at things like the effective ages of buildings that had been rehabilitated. Nexus did find some uniformity issues and revalued the fast-food restaurants for the 2007 annual adjustment. With that revaluation, the subject property's relative position among fast-food restaurants changed. While the subject property had been assessed at less than the average for fast-food restaurants in 2006, it was assessed above that average in 2007. *Wuensch testimony.*

**C. Valuation opinions**

22. Each party offered expert witnesses who gave opinions about the subject property's market value. Davis-Gratner called two appraisers—Daniel Semler and Jay Allardt.[7] The Assessor in turn called its own appraiser, James Cecil, as well as Jeff Wuensch.

**1. Daniel Semler**

23. Mr. Semler has worked as an appraiser since 1970. He is an S.R.A.—a designation awarded by the Appraisal Institute that originally meant "senior residential appraiser." He is also a certified general appraiser. That certification allows him to appraise any type of property, although only about 15% to 20% of his practice involves commercial

[7] Davis-Gratner also called Sheila Murray, a level II certified assessor-appraiser employed by the law firm that represented Davis-Gratner. Among other things, Ms. Murray compared the subject property's assessment to the assessments of other properties containing KFC restaurants. But she did not offer an opinion of the subject property's market value-in-use.

property.  Other than the subject property, Mr. Semler has only appraised two or three fast-food restaurants. *Pet'r Ex. 5*.

**a. Semler's cost-approach analysis**

24. Mr. Semler prepared an appraisal report in which he estimated the value of a fee simple interest in the subject property as of January 1, 2005. *Semler testimony; Pet'r Ex. 5 at 1, 28*. To arrive at his ultimate value estimate of $335,000, he considered all three generally accepted valuation approaches—the cost, sales-comparison (which he referred to as the "market approach"), and income approaches. *Semler testimony, Pet'r Ex. 5*.

25. Under his cost-approach analysis, Mr. Semler first estimated the replacement cost new for the restaurant building. To do that, he turned to the cost data for class-C restaurants of average-to-good construction quality published by Marshall Valuation Service. He made similar calculations for the property's site improvements. But he did not include the property's utility building, explaining that he did not feel that the building contributed to the property's value for commercial uses. *Semler testimony; Pet'r Ex. 5 at 10-11*.

26. Mr. Semler then considered the restaurant building's depreciation, which he classified into two separate categories: physical depreciation and obsolescence. To determine physical depreciation, he estimated an effective age of 20 years, which he then divided by 35 years—the economic life that Marshall Valuation Service suggests for average-to-good class-C restaurants. That yielded physical depreciation of 57%. *Semler testimony; Pet'r Ex. 5 at 11-12*.

27. Mr. Semler next examined whether the restaurant building suffered from functional or economic obsolescence. Although Mr. Semler did not find any obsolescence for the building's current use as a KFC restaurant, he explained that almost all other uses would require significant changes in the building's appearance and floor plan. He estimated the costs for those changes to be at least 15% of the building's replacement cost new, or $89,250. *Semler testimony; Pet'r Ex. 5 at 12*.

28. After analyzing the property under the income approach, however, Mr. Semler concluded that the subject property suffered from additional functional obsolescence because the improvements were not generating sufficient market rent to support the land's value at its highest-and-best use. He attributed that to how the building was situated on the lot, which resulted in a significant amount of green space that was not being used for any purpose. Although Mr. Semler would have preferred to quantify his adjustment through adequate rental data, he did not have that data. Thus, he estimated an amount of obsolescence—15% of the land value or $52,000—that corresponded to the percentage of the land that was not being used. *Semler testimony; Pet'r Ex. 5 at 12-13, 24*.

29. All told, Mr. Semler felt that the building's depreciated replacement cost should be reduced by an additional $141,250 to account for functional obsolescence. *Semler testimony*. That was actually less than what Mr. Semler indicated in his appraisal report where he had mistakenly double counted the $89,250 adjustment for converting the building to another use. *Semler testimony*; *Pet'r Ex. 5 at 12-13*.

30. To estimate the subject land's value, Mr. Semler looked at sales of nine other properties. All were from New Castle and several were on Memorial Drive. He ultimately settled on a land value of $345,000, which, when added to his corrected estimate for the improvements, yielded a total cost-approach estimate of $489,600. *Semler testimony*; *Pet'r Ex. 5 at 13-18*.

**b. Semler's sales-comparison analysis**

31. For his sales-comparison analysis, Mr. Semler looked at properties located near the subject property because he believed that location differences were the most difficult adjustments to quantify. He came up with four sales from New Castle. The first property had been a Subway restaurant, but it was sold for use as a franchise fried-chicken restaurant. The second had been a Ponderosa steakhouse that the buyer converted to a sports bar and restaurant. The third was sold for continuing operation as a fast-food

restaurant. And the fourth had been a Hardee's fast-food restaurant that was vacant at the time of the sale. Mr. Semler adjusted each property's sale price, largely to account for differences between it and the subject property in terms of the size and age of the buildings and the value of the lot. Although the sales occurred in 1999, 2003, 2004, and 2006, Mr. Semler did not adjust the sale prices to relate to January 1, 2005, because he believed that the New Castle market had been "pretty flat" between 1999 and 2006. *Semler testimony; Pet'r Ex. 5 at 18-21.*

32. Mr. Semler's adjusted sale prices ranged from $117.69 to $174.40 per square foot of building space. Mr. Semler, however, noted that the two highest prices ($174.40/sq. ft and $161/sq. ft.) were for the first and third properties. Unlike the subject property, those two properties were being used for their highest and best use. Mr. Semler therefore further adjusted those sale prices, which lowered his range to $117.69 to $159.40. In light of the subject building's age he further narrowed the likely value range to $118 to $140 per square foot and estimated the subject property's value at roughly the mid part of that range, or $450,000. *Pet'r Ex. 5 at 20.*

**c. Semler's income-approach analysis**

33. For his analysis under the income approach, Mr. Semler estimated market rent, which he then capitalized to reach a value conclusion. Because, in Mr. Semler's words, the subject property was "owner occupied," he did not consider any rent that the owners paid themselves as relevant to his determination. He instead looked to four comparable leased properties to estimate what he described as the subject property's "net" market rent. *Pet'r Ex. 5 at 21-22; Semler testimony.*

34. For three of those four properties, either the landlord or tenant had asked Mr. Semler to keep their rental information confidential; so he did not offer many details. The net rents ranged from $6.08 to $11.80 per square foot, but the property with the highest rent was in better condition than the subject property. Mr. Semler also considered net rents for Famous Recipe chicken restaurants from Richmond and Connersville, all of which were

newer and smaller than the subject restaurant building. The Famous Recipe restaurants had net rents ranging from $13.83 to $24.50 per square foot, but Mr. Semler found little consistency between them. For example, the building with the least desirable location had the highest rent. Mr. Semler therefore did not rely on the Famous Recipe restaurants other than to illustrate that a specific user may be willing to pay more for a building than another user. Ultimately, Mr. Semler settled on net market rent of $26,250 ($7.50/sq. ft.) for the subject property. *Semler testimony; Pet'r Ex. 5 at 21-22.*

35. Mr. Semler explained that there are different ways to determine an appropriate capitalization rate. One method is to extract a rate from market sales. Unfortunately, only one property that Mr. Semler examined in his sales-comparison analysis yielded a capitalization rate. That rate was between 9% and 10%. Nonetheless, based on discussions with other appraisers and published materials, Mr. Semler felt that 9% to 10% was an appropriate range for the subject property. When applied to the subject property's net market rent, those rates yielded a value range of $262,500 to $291,667. *Semler testimony; Pet'r Ex. 5 at 22-25.*

36. Mr. Semler also determined a capitalization rate using the band-of-investment method, which considers both a typical investor's desired rate of return on equity and the cost of the investor's borrowed money. Mr. Semler believed that an investor seeking to buy the subject property could have gotten a 15-year loan at 7.5% with a 75% loan-to-value ratio. Those numbers translated to a capitalization rate of 10.84% and a value of $242,159. *Semler testimony; Pet'r Ex. 5 at 22-23.*

**d. Semler's reconciliation of values**

37. In reconciling his value estimates under the three approaches, Mr. Semler found that his conclusions under the cost approach were only a "fair" indication of the property's value because the improvements did not reflect the property's highest and best use. *Semler testimony; Pet'r Ex. 5 at 25.* Similarly, in his appraisal report, Mr. Semler explained that the sales from his sales-comparison analysis were "adequate but not good," because they

required major adjustments, many of which were based on his judgment rather than on market information. *Id. at 26*. At the hearing, though, Mr. Semler described his comparable sales as "surprisingly good." *Semler testimony*.

38. In any event, Mr. Semler gave the greatest weight to his conclusions under the income approach, which he explained is typically the best approach for valuing income-producing properties. He acknowledged that the major problem under that approach is estimating market rent and that even small errors in doing can lead to large differences in an appraiser's value conclusion. While the rents for older restaurants along Memorial Drive and the newer, smaller chicken restaurants from Richmond and Connersville differed significantly, Mr. Semler felt that the rents for the older local restaurants best reflected the subject property's market. *Semler testimony; Pet'r Ex. 5 at 26*.

39. While, in Mr. Semler's view, a prudent investor likely would pay little more than the highest value estimated under his income-approach analysis ($281,667), the subject land alone was worth $345,000. Under those circumstances, Mr. Semler believed that an investor would pay an amount equal to the land's values minus the cost of razing the subject buildings ($10,000). Mr. Semler therefore estimated the subject property's market value at $335,000 as of January 1, 2005. *Semler testimony; Pet'r Ex. 5 at 28.* Because he believed that property values remained steady or even declined slightly between that date and January 1, 2006, he estimated that the subject property would have been worth the same amount as of January 1, 2006. *Semler testimony; Pet'r Ex. 5A*.

**2. James Cecil**

40. James Cecil is a self-employed certified residential appraiser. He has only worked as an appraiser since 2003, although he worked in the banking industry for 30 years before that. Mr. Cecil's license allows him to appraise certain non-complex commercial properties, such as owner-occupied or single-tenant properties. He has appraised approximately 80 commercial properties, but only two properties of the same type as the subject property. *Cecil testimony*.

41. Mr. Cecil estimated the market value of a fee simple interest in the subject property as of January 1, 2005. *Resp't Ex. 10 at 6, 38; Cecil testimony*. Under a heading in his appraisal report entitled "Reconciliation of Market Value, and Market Value in Use, Mr. Cecil explained:

> The state of Indiana defines market value in use of a property to be value obtainable by the owner from the properties [sic] current use as reflected by the utility received by the owner or similar users. Since the owner of the subject property is also the operator of the business located on that property, the market value in use to the owner-operator is also the same as the value in use received by the owner-operator or that would be received by another investor who intended not just to own the subject property but also to operate said property as a fast food restaurant.

*Resp't Ex. 10 at 7*.

42. Mr. Cecil did not have full access to the subject property; he had been told that he would not be welcome. He therefore observed the restaurant building's exterior and essentially posed as a customer to make a limited inspection of its interior. *See Resp't Ex. 10 at 20; Cecil testimony*.

**a. Cecil's cost-approach analysis**

43. Like Mr. Semler, Mr. Cecil considered all three generally accepted valuation approaches. For his cost-approach analysis, Mr. Cecil used Marshall Valuation Service data for a class-C fast-food restaurant of "very good" construction. *Resp't Ex. 10 at 25*. To estimate the restaurant building's physical depreciation, Mr. Cecil began with a typical life expectancy of 60 years, which he said that he got from Marshall Valuation Service. *Cecil testimony; Resp't Ex. 10 at 26*. He then estimated the building's effective age at six years, due to "good maintenance, upkeep and remodeling." *Resp't Ex. 10 at 26*. When questioned on cross-examination, however, Mr. Cecil admitted that he did not know the ages of the building's major components, including the foundation, plumbing, electrical system, siding, roof, and internal walls. *Cecil testimony*. By using such a long economic

life and short effective age, Mr. Cecil estimated the building's physical depreciation at only 10 %. And he did not find any functional or external obsolescence. *Id.; Resp't Ex. 10 at 26*.

44. To estimate the subject land's value, Mr. Cecil looked at five sales—three from Memorial Drive, one from just off Memorial Drive, and one from Anderson. Those sale prices ranged from $1.92 to $37.51 per square foot. For one of those sales, Mr. Cecil actually used the capitalized value of a ground lease involving a Pizza Hut restaurant. Mr. Cecil settled on a land value of $6.29 per square foot or $410,988.60. In total, Mr. Cecil's cost-approach analysis led him to estimate the subject property's value at $1,110,000. *Cecil testimony*; *Resp't Ex. 10 at 26-28*.

**b. Cecil's sales-comparison analysis**

45. For his sales-comparison analysis, Mr. Cecil relied on seven sales of fast-food restaurants, none of which were from New Castle. Mr. Cecil gave three reasons for looking at sales from other cities: (1) he felt that the market for fast-food restaurants extended beyond New Castle, with many buyers coming from other states and even other countries; (2) he was able to use traffic counts to adjust sale prices to account for location-based differences; and (3) he found no sales of similar properties from New Castle. *Cecil testimony; Resp't Ex. 10 at 31-32.*

46. Mr. Cecil used more than the minimum number of sales because he wanted to make sure that he relied on valid sales that did not include personal property and in which fee simple title had transferred. Nonetheless, if any of the sales turned out to be invalid, he felt that using a greater number of sales would offset the invalid sale's influence. Mr. Cecil investigated each sale's validity by talking to the assessor's office in the county in which the sale occurred. He also called the parties to each sale, although none of them called him back. Even if the parties had told him there was a contemporaneous lease on a property and that it was classified as "sale-lease value," Mr. Cecil might still have used the sale after looking into the possibility of making adjustments. *Cecil testimony*.

47. Despite those precautions, Mr. Cecil admitted on cross-examination that he had not accounted for the fact that one of his comparable sales (sale # 7) had involved personal property as well as real estate. *Cecil testimony*. In his analysis, Mr. Cecil had used a sale price of $820,000, but the disclosure form for that transaction indicated that $480,000 of that price was attributable to personal property. *Pet'r Ex. 12G*. Mr. Cecil also found an error in the sale price he had used for another property (sale # 6), but explained that he had not given that sale price much weight in his sales-comparison analysis. *Cecil testimony*.

48. The comparable properties' adjusted sale prices ranged from $231.71 to $539.27 per square foot. Mr. Cecil found sale numbers 1, 2, 4 and 7 to be most comparable to the subject property, and he used the average of those prices ($309.83/sq. ft.) to estimate its value. Thus, Mr. Cecil ended up with a sales-comparison estimate of $1,100,000 for the subject property. *Resp't Ex. 10 at 32*.

**c. Mr. Cecil's income-approach analysis**

49. For his analysis under the income approach, Mr. Cecil estimated market rent by looking at four properties—one each from Memorial Drive and Anderson, and two from Muncie. He assumed a one-year lease with the owner being responsible for insurance and taxes. Mr. Cecil concluded that restaurants in the subject property's area have typically rented for $14.00 to 18.76 per square foot depending on various factors, such as the age and size of the improvements, the lot size, and the property's location. Because the subject property was owner-occupied, Mr. Cecil selected a number ($18.00/sq. ft.) at the high end of that range. He then used two mortgage-equity techniques to estimate a capitalization rate of 7.5%, which when applied to his estimated net operating income, yielded a value of $750,000. *Cecil testimony; Resp't Ex. 10 at 34-35*.

**d. Mr. Cecil's reconciliation**

50. Ultimately, Mr. Cecil gave no weight to his conclusions under the income approach. He explained that the income approach strongly indicates value where an investor owns property mainly for its rental income and there is good rental data available. Mr. Cecil, however, believed that the subject property's owners primarily focused on earning income through operating a fast-food restaurant. He felt that a value-in-use estimate would have been more reliable for the subject property, but only if he had historical financial data about the restaurant's operations. And he did not have that data. *Cecil testimony; Resp't Ex. 10 at 37-38.*

51. Thus, Mr. Cecil gave the greatest weight to his sales-comparison analysis. In his view, that approach was the most consistent with a prudent buyer's thought processes for a property like the subject property. He also found that his conclusions under the cost approach supported his ultimate estimate of $1,100,000. *Cecil testimony; Resp't Ex. 10 at 37-38.*

52. When asked about the subject property's value as of March 1, 2007, Mr. Cecil explained that the value increased 1.5% to approximately $1,130,000. *Cecil testimony*; *Resp't Ex. 12*. He based that conclusion on sale #6 from his sales-comparison analysis. That property sold twice between August 2006 and August 2007, with an approximately 1.5% increase in its sale price. *Cecil testimony*.

**3. Jeff Wuensch**

53. As already explained, Jeff Wuensch is the co-owner of Nexus Group. Nexus consults primarily with county assessors and works in approximately 25 of Indiana's 92 counties. Nexus deals with every aspect of the assessment process, from valuing properties to handling appeals and performing ratio studies. The Department of Local Government Finance ("DLGF") has certified Mr. Wuensch as a level I and II assessor-appraiser. He is also member of the International Association of Assessing Officers ("IAAO"), which has

certified him to teach classes. And before helping to found Nexus, Mr. Wuensch was the Director of Tax Review for the DLGF's predecessor agency, the State Board of Tax Commissioners. *Wuensch testimony.*

54. In response to Davis-Gratner's appeal of the subject property's 2006 assessment, the Assessor asked Nexus to consider additional information relating to the property's value. Mr. Wuensch therefore asked Brad Berkemeier, a Nexus employee, to search LoopNet for data on fast-food restaurants. LoopNet is a source used by real estate brokers and investors. Mr. Berkemeier compiled a list of 31 sales throughout Indiana. The list included both restaurants that were vacant at the time of sale and ones that were occupied. All of the vacant restaurants sold for less than the subject property's 2006 - 2007 assessments, but 16 of the 18 occupied restaurants sold for more. And when compared as a function of price per square foot of building area, all 18 occupied restaurants sold for more than the subject property's 2006 assessment. *Wuensch testimony; Resp't Ex. 6.*

55. Mr. Wuensch also contacted the IAAO and asked whether it had any information from publications or course materials to assist in valuing the subject property. The IAAO referred him to something he already had—a paper titled "*The Valuation of Fast Food Restaurants*" contained in an IAAO journal. The paper's author held designations as a MAI, which Mr. Wuensch testified was the highest designation given by the Appraisal Institute, and a CAE, the highest certification offered by the IAAO. *Wuensch testimony; Resp't Ex. 8*.

56. The paper discusses all three generally accepted valuation approaches in the context of valuing fast-food restaurants. Mr. Wuensch focused on the following two passages:

> The application of the income approach to fast food properties parallels that of other commercial property. A market rent is estimated. Percentage rents are common for fast food restaurants and range from 6% to 8% on a net basis. Therefore, if the subject has sales volume of $800,000 per year, the range for annul rent for the subject would be $48,000 ($12.43 per square foot on a net basis) to $64,000 ($16.57 per square foot) for a 3,862 square foot property. . . .

> An analysis should be made for the development costs as they relate to an imputed rental amount. Assume that the depreciated replacement cost new plus land value for a 3,862 square foot fast food restaurant is $679,000 in the cost approach. Rents for sale leasebacks will typically be 11% to 12% of cost on a net basis. Considering a fast food use, 12% may be used as a result of the short-lived components of typical buildings. Thus, $679,000 multiplied by 12% equals $81,480 or $21.10 per square foot on a net basis. This method may provide a "check" to support an estimate for comparable market rents.

*Resp't Ex. 8 at 6-7*. According to Mr. Wuensch, appeals from Captain D's, another fast-food restaurant in New Castle, as well as from two fast-food restaurants in Marion and Hancock Counties, supported the paper's methodology of estimating market rent as a percentage of gross sales. In fact, he was told by the owner of Captain D's that franchisees often pay rent equal to 6% of sales. *Wuensch testimony*.

57. Relying on the IAAO paper, Mr. Wuensch estimated the subject property's gross market rent as between 6% and 8% of Restaurant Services' annual sales. He admitted that expenses should be deducted, but he had been unable to determine appropriate expenses because he had not seen Restaurant Services' financial information until the Board's hearing. Mr. Wuensch then capitalized his estimated gross rent using capitalization rates from the appraisals prepared by Semler and Cecil and from LoopNet data. The resulting values ranged from $ to $ . Mr. Wuensch also noted that the paper's second technique—imputing income as 11% to 12% of cost—supported the subject property's assessments. Eleven percent of the subject property's stipulated 2006 assessment is $68,156, which when capitalized using any of the above-referenced rates exceeds the property's 2006 assessment. *Wuensch testimony; Resp't Ex. 19*.

**4. Jay Allardt**

58. Mr. Allardt is a certified general appraiser and an SRA. He is also a member and former officer of the Hoosier chapter of the Appraisal Institute. Mr. Allardt began appraising commercial properties more than 25 years ago, and for the last 15 years, those properties

have made up 75%-80% of his business. He spends the balance of his time working with properties in litigation and appraising agricultural and complex residential properties. Mr. Allardt has also appraised various fast-food restaurants in his career. At the time of the hearing, he was working on four such appraisals and he had appraised another four fast-food restaurants the previous year. *Allardt testimony*.

**a. Allardt's review of the other experts' opinions**

59. Mr. Allardt reviewed and analyzed the valuation opinion of each expert witness, beginning with Mr. Cecil. According to Mr. Allardt, Mr. Cecil purported to value a fee simple interest in the subject property, but by relying almost exclusively on sale-leaseback transactions, he actually valued a leased-fee interest instead. *Allardt testimony*.

60. Mr. Allardt viewed that as significant because sales involving leased fees might include things other than just real estate, such as amounts attributable to the lessee's business enterprise or fixtures and equipment. According to Mr. Allardt, many sale-leaseback transactions in which a leased fee interest is transferred include those other items. In most sale-leasebacks, the seller essentially sells all or a portion of the income generated from its business, including the income attributable to its equipment, its assembled and trained workforce, and the quality of its management. In that sense, sale-leasebacks are essentially financing transactions in which a business can get what amounts to a loan of up to 100% of the value of its entire enterprise. By contrast, a business typically can get only 80% of the value of its real estate under more conventional financing. Thus, when the owner sells the property and signs a long-term lease, the lease payments are determined by what is necessary to repay the loan, not by the real estate's market rent. *Allardt testimony.*

61. Mr. Allardt also explained that sale-leaseback transactions often include multiple properties bundled together for sale. In those cases, the parties may arbitrarily assign values to the individual restaurants. Appraisers therefore cannot simply extract individual sale prices from those sales disclosures. *Allardt testimony*.

62. Turning to Mr. Cecil's sales-comparison analysis, Mr. Allardt explained that Mr. Cecil's first six sales all appeared to be sale-leasebacks. The parties were companies such as CNL Funds and Realty Income Corp. that commonly deal in sale-leasebacks. *Allardt testimony; Resp't Ex. 10; Pet'r Exs. 12A-12G*. CNL's own website explains that fact. *Allardt testimony*. Also, two of the sales disclosures list the same address for the buyer and seller, an indication that the sales may not have been at arm's length. *Allardt testimony; Pet'r Exs. 12A-12B*. In addition, Mr. Cecil himself acknowledged his $820,000 sale price for comparable sale #7 included $480,000 that the parties had attributed to personal property. Thus, after removing that sale, Mr. Cecil's sales-comparison analysis valued only a leased fee interest in the subject property. *Allardt testimony*.

63. Mr. Allardt had just as many reservations about Mr. Cecil's cost-approach analysis. According to Mr. Allardt, Mr. Cecil used Marshall Valuation Service's cost data for a class-C fast-food restaurant in "very good" condition when Mr. Cecil himself admitted that the building was only in "good" condition. Next, in estimating the subject building's physical depreciation, Mr. Cecil did three things that caused Mr. Allardt serious concern: (1) he used a 60-year economic life expectancy, (2) he estimated an effective age of only six years, and (3) he did not recognize any functional obsolescence. *Allardt testimony*.

64. As to the first point, Marshall Valuation Service provides a 30-year economic life for a class-C fast-food restaurant in good condition. *Allardt testimony; Pet'r Ex. 17*. Using an economic life of 60 years dramatically affected Mr. Cecil's conclusions. *Allardt testimony*.

65. Second, the subject building was constructed in 1967, making it 38 years old as of the January 1, 2005, valuation date for the 2006, assessment. Yet Mr. Cecil estimated its effective age at only six years. Mr. Allardt did not see how that was even possible. Although Mr. Allardt acknowledged that he did not know what the remodeling in 2004 entailed, he explained that the subject property's effective age would be 29 years under

the Guidelines, which provide a table (table F-2 in Appendix F) for converting a building's actual age to an effective age based on its condition. If one uses an economic life of 35 years—the life for a dining/lounge building provided by the Guidelines—that 29-year effective age translates to 70% physical depreciation. That number is very close to what Mr. Allardt came up with using the 30-year life expectancy from Marshall Valuation Service and an effective age of 20. *Allardt testimony*.

66. Third, despite Mr. Cecil's failure to recognize it, Mr. Allardt felt that the subject building suffered from functional obsolescence. According to Mr. Allardt, there have been essentially three generations of fast-food restaurants. The first generation consisted of walk-up restaurants. The second generation featured walk-in dining with the counter in front and seating to one side. Many second-generation restaurants did not have drive-through service when they were built. The third generation is a more efficient design. Buildings are narrower and situated lengthwise on lots to allow cars to stack for drive-through service and menu boards to be optimally placed. Dining areas are in front of the counter so workers can monitor the area for cleanliness. In Mr. Allardt's eyes, the subject building resembles a second-generation restaurant; it is situated on the southeast corner of the lot, leaving no stacking room for cars. Mr. Allardt therefore recognized 15% functional obsolescence. *Allardt testimony*.

67. Mr. Allardt also took issue with Mr. Cecil's analysis of the subject land's value. Mr. Cecil did not use the Steak n' Shake or White Castle sites (comparables # 6 and #9 from Mr. Semler's appraisal) even though both were located near the subject property and the Steak n' Shake site was very close to the subject property's size. *Allardt testimony; see also Pet'r Ex. 5 at 15-16.* Plus, in Mr. Allardt's view, Mr. Cecil relied on two bad pieces of information: a sale to McDonald's (sale # 3) and the Pizza Hut ground lease. Because McDonald's needed the property to build a new store on an adjacent parcel, Mr. Allardt viewed that sale as something less than an arm's-length transaction. And the Pizza Hut lease was not strictly a land lease. The Pizza Hut is actually part of a strip center, and the developer spent significant money to develop the site. Mr. Cecil used a 1999 lease, but a

later 2001 lease includes access to a drive-up lane, common areas, and parking. *Allardt testimony*.

68. Interestingly, although Mr. Cecil gave his income-approach analysis no weight, Mr. Allardt viewed it as the most reliable of Mr. Cecil's approaches. Mr. Allardt agreed with Mr. Cecil's estimate for the range of market rents. Despite the fact that his rental comparables were smaller and newer that the subject property, however, Mr. Cecil, chose rent at the high end of that range. Mr. Allardt, by contrast, felt that an appropriate market rent was at the low end of that range. *Allardt testimony*.

69. Mr. Allardt was also very skeptical of Mr. Wuensch's valuation opinions. First, Mr. Allardt explained that the LoopNet data compiled by Nexus was unreliable for valuing the subject property. It lacked key information, such as the rights conveyed in each sale, the age of the improvements, and the land values for the various locations across the state. *Allardt testimony; Respondent's Ex. 6*.

70. Mr. Allardt was equally troubled by Mr. Wuensch's reliance on the IAAO paper. While Mr. Allardt found the paper's premise that market rent can be estimated based on gross sales interesting, the paper did not explain how that theory related to New Castle. And the paper did not test its conclusions. For example, the paper dealt in averages, but it did not say whether its statement that market rents fell between 6% and 8% of gross sales held true at the margins. That was important for the subject property because Restaurant Services' gross sales were at the high end. In short, Mr. Allardt believed that the paper offered a "broad brush" methodology that had not been shown to apply to the subject property. *Allardt testimony*.

71. Mr. Semler's appraisal drew less criticism from Mr. Allardt. Nonetheless, Mr. Allardt explained that Mr. Semler should have used the Marshall Valuation Service cost data for fast-food restaurants instead of the data for general restaurants. Mr. Semler also recognized more functional obsolescence than Mr. Allardt did. Even so, Mr. Allardt

credited Mr. Semler for at least recognizing that the property suffered from functional obsolescence, something that Mr. Cecil did not do. *Allardt testimony*.

**b. Allardt's own valuation opinion**

72. Mr. Allardt did not just analyze the other experts' opinions; he also offered his own valuation opinion. While Mr. Allardt did not prepare a written appraisal report, he explained that USPAP allows an appraiser to give an oral valuation opinion if he has file memoranda from which he can produce a written report with enough information to lead someone to a value opinion. Mr. Allardt testified that his files contained ample support for his opinion, although he also said that his notes were not for distribution. *Allardt testimony*.

73. For his cost-approach analysis, Mr. Allardt estimated the restaurant building's depreciation at 70%. Given the building's age and condition, both the Guidelines' depreciation schedules and Marshall Valuation Service's data supported that number. Mr. Allardt then estimated the subject land's value at $350,000. To reach that number, he relied on the sales of two nearby parcels—the White Castle and Steak n' Shake sites. Those two parcels sold for $308,000 and $325,000, respectively. All told, Mr. Allardt estimated the property's market value at $495,000 under the cost approach. *Allardt testimony*.

74. For his sales-comparison analysis, Mr. Allardt relied primarily on three sales:

- A 23-year-old Rax roast beef restaurant in Richmond that sold on July 7, 2005, for $472,500. The buyer used the property to operate an Arby's. The land was more valuable than the subject land and it was an arm's-length sale.

- A property directly across the street from the subject property on a slightly smaller site that sold for $325,000. It had been used as an insurance office, but the buyer spent $255,510 to convert the building to a Subway restaurant.

- A Rax restaurant that sold for $385,000 on April 22, 2005. It was built in 1986 and sits on 1.38 acres on the main drag in Shelbyville.

*Allardt testimony.* While Mr. Allardt acknowledged that the second sale was not ideal because he had to add two numbers together, he had appraised the property for the buyer and he was confident of the numbers. *Id.* Based on those sales and his adjustments, Mr. Allardt estimated the subject property's market value-in-use at $462,500 as of January 1, 2005. *Id.*

75. In explaining his analysis under the income approach, Mr. Allardt noted the wide disparity between the market rent estimated by Messrs. Semler and Cecil ($7.50/sq. ft. and $18/sq. ft.). Mr. Allardt felt that the property's true market rent lay between those two estimates at $14 to $15 per square foot. He found a range of capitalization rates between 9% and 9.5%, but leaned more heavily toward the higher rate because owners of single restaurants have a more difficult time spreading risk. He therefore estimated the subject property's market value at $495,000 using the income approach. *Allardt testimony*.

76. In reconciling his conclusions, Mr. Allardt gave the greatest weight to his analyses under the sales-comparison and income approaches. He concluded that the subject property was worth $480,000 as of January 1, 2005. He then used Mr. Cecil's appreciation rate of 1.5% to estimate a value of $487,200 as of January 1, 2006. *Allardt testimony*.

## CONCLUSIONS OF LAW AND ANALYSIS

### A. Burden of proof

77. A taxpayer seeking review of an assessing official's determination must make a prima facie case proving both that the current assessment is incorrect and what the correct assessment should be. *See Meridian Towers East & West v. Washington Twp. Assessor*, 805 N.E.2d 475, 478 (Ind. Tax Ct. 2003); *see also, Clark v. State Bd. of Tax Comm'rs*, 694 N.E.2d 1230 (Ind. Tax Ct. 1998).[8] If a taxpayer meets that burden, the assessing official must offer evidence to impeach or rebut the taxpayer's evidence. *See American United Life Ins. Co. v. Maley*, 803 N.E.2d 276 (Ind. Tax Ct. 2004); *Meridian Towers,* 805 N.E.2d at 479. But the burden of persuasion remains at all times with the taxpayer. *Thorntown Tel. Co. v. State Bd. of Tax Comm'rs*, 629 N.E.2d 962, 965 (Ind. Tax Ct. 1995).

78. The taxpayer's burden of proof, however, must be viewed in the context of Indiana's assessment system. Indiana assesses real property based on its true tax value, which the 2002 Real Property Assessment Manual defines as "the market value-in-use of a property for its current use, as reflected by the utility received by the owner or a similar user, from the property." 2002 REAL PROPERTY ASSESSMENT MANUAL at 2 (incorporated by reference at 50 IAC 2.3-1-2). To determine a property's true tax value, Indiana assessing officials generally use a mass-appraisal version of the cost approach set forth in the Real

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[8] Effective July 1, 2009, the Indiana General Assembly amended Ind. Code § 6-1.1-15-1 to add subsection (p), which provides:

> This subsection applies if the assessment for which a notice of review is filed increased the assessed value of the assessed property by more than five percent (5%) over the assessed value finally determined for the immediately preceding assessment date. The county assessor or township assessor making the assessment has the burden of proving that the assessment is correct.

Ind. Code § 6-1.1-15-1; P.L. 182-2009(ss) § 111. Although the subject property's assessment increased by more than 5% each year between 2005 and 2007, Davis-Gratner does not argue that the amendment applies to this appeal. The Assessor, however, addressed that question, arguing that the amendment applies only prospectively and does not shift the burden of proof in this case because Davis-Gratner filed its appeal petitions before the amendment's effective date. The Board need not decide that question. As explained below, the parties offered ample evidence to show that the assessment was incorrect, and the Board finds Mr. Allardt's valuation opinion persuasive. Thus, the Board would reach the same result no matter who bore the burden of proof.

Property Assessment Guidelines for 2002 – Version A. That Guidelines-based determination is presumed to be accurate. *See* MANUAL at 5; *Eckerling v. Wayne Twp. Assessor,* 841 N.E.2d 674, 676 (Ind. Tax Ct. 2006). A taxpayer, however, may rebut that presumption with evidence that is consistent with the Manual's definition of true tax value. MANUAL at 5. A market-value-in-use appraisal prepared according to the Uniform Standards of Professional Appraisal Practice ("USPAP") often will suffice. *Id.; Eckerling,* 841 N.E.2d at 678. A taxpayer may also offer actual construction costs, sales information for the subject or comparable properties and any other information compiled according to generally accepted appraisal principles. MANUAL at 5.

79. Regardless of the method used to rebut an assessment's presumed accuracy, a party must explain how its evidence relates to the subject property's market value-in-use as of the relevant valuation date. *O'Donnell v. Dep't of Local Gov't Fin*., 854 N.E.2d 90, 95 (Ind. Tax Ct. 2006); *see also Long* 821 N.E.2d at 471. For March 1, 2006, assessments, that valuation date was January 1, 2005. 50 IAC 21-3-3. For March 1, 2007, assessments, it was January 1, 2006. *See id.*

**B. Discussion**

80. Between them, the parties offered four expert opinions, three of them by licensed appraisers who testified that they followed USPAP in reaching their conclusions. And each expert largely testified as to how his valuation opinion related to the relevant valuation dates.[9] Thus, the Board must weigh those various opinions to determine which one most reliably estimates the subject property's market value-in-use.

[9] Although apparently attempting to provide a valuation opinion for the property's 2007 assessment, Mr. Cecil referred to the property's value as of March 1, 2007. *Cecil testimony, Resp't Ex. 12*. As explained above, the relevant valuation date for that assessment was January 1, 2006.

### 1. Mr. Wuensch's opinion

81. The Board starts with Mr. Wuensch's opinion. Mr. Wuensch has significant training and experience in mass appraisal, but he is not a licensed appraiser. While Mr. Wuensch's opinion is still relevant, his lack of appraisal training does affect its weight in determining the question at hand—the market value-in-use of an individual property.

82. More importantly, the Board is not persuaded by the data, assumptions, and judgments underlying Mr. Wuensch's opinion. First, the Board notes that much of Mr. Wuensch's testimony addressed how the subject property and other fast-food restaurants were assessed in the mass-appraisal process. The assessment may have been presumptively accurate, although Davis-Gratner contests that notion on grounds that Nexus departed substantially from the Guidelines. In any event, the valuation opinions of three different licensed appraisers amply rebutted that presumption. The Board therefore gives Mr. Wuensch's testimony about how Nexus assessed the subject property and other fast-food restaurants little weight.

83. The Board similarly gives little weight to Mr. Wuensch's testimony about the sales information for other fast-food restaurants compiled from LoopNet. As Mr. Allardt noted, neither Mr. Wuensch nor Mr. Berkemeier did much to compare those properties to the subject property. For example, they did not address key information, such as the rights conveyed in each sale, the age of improvements or the land values for the various locations across state. And Mr. Wuensch did not even purport to form a value conclusion from that information, except perhaps to generally claim that the subject property was assessed at a reasonable level.

84. Mr. Wuensch, however, did offer a valuation opinion tied specifically to the subject property—his income-approach estimate derived from Restaurant Services' gross sales. Relying on the IAAO paper, Mr. Wuensch estimated the property's rent at 6% to 8% of gross sales. He then capitalized that rent using the rates proposed by Messrs. Semler and Cecil and one taken from LoopNet data.

85. But Mr. Wuensch admitted that, to apply the income approach properly, he needed to deduct expenses from his estimated gross rent before capitalizing that rent. Mr. Wuensch blamed his failure to deduct expenses on the fact that he did not see Restaurant Services' sales and expense data until the beginning of the hearing. While that may be true, it is because the Assessor chose to subpoena those documents to the hearing rather than ask for them in discovery.

86. The Assessor tried to cure that glaring problem with Mr. Wuensch's opinion by offering a modified version of Mr. Wuensch's analysis in her post-hearing brief. First, she determined what she viewed as appropriate expenses. Thus, she estimated $ for "variable expenses," which she took from Davis-Gratner's Form 8825 federal tax return for the tax year ending on May 31, 2006. *Assessor's Post-Hearing Brief at 22 n. 7; Pet'r Ex. 6*. That reflected all of the expenses listed on the return other than depreciation and property taxes, because according to the Assessor, the lease between Davis-Gratner and Restaurant Services made Restaurant Services responsible for taxes. *Id*. The Assessor further estimated maintenance reserves equaling 3% of effective gross income. She took that amount from a sample table in the IAAO paper because she felt that the amount that Davis-Gratner attributed to maintenance reserves in its sales and expense statements was inadequate. *Id. at n. 8*. Because the property was leased, however, the Assessor did not recognize anything for vacancy and collection loss. *Id. at n. 5*.

87. Having determined expenses, the Assessor performed three separate calculations using potential gross income based on 6%, 7%, and 8% of store sales, respectively. She then capitalized the resulting net operating income under each scenario using a 7.5% capitalization rate. The calculation based on 7% of gross sales—the midpoint suggested by the IAAO paper—yielded a capitalized value of $ (rounded). The Assessor therefore asked the Board to raise the subject property's assessment to that amount. *Assessor's Post-Hearing Brief at 23.*

88. The Board gives little weight to either Mr. Wuensch's opinion or the calculations that the Assessor offered in her post-hearing brief. As already explained, Mr. Wuensch admitted that his opinion was inaccurate because he had not deducted any expenses from his estimated gross rent. And the Assessor's calculations did not cure that problem. While the income approach involves mathematical formulas, the numbers used in those formulas are determined by exercising informed judgment. And the judgments reflected in the Assessor's brief did not come from any witness who testified subject to cross-examination. For example, no expert testified that it would be appropriate to use purportedly market-derived information to estimate the subject property's income, but simply use Davis-Gratner's actual reported expenses without testing them against comparable properties' expenses. Similarly, it is not self-evident that an appraiser would necessarily ascribe zero vacancy and collection loss to the property simply because it is subject to a lease that will expire in less than 10 years. And the Assessor is wrong in claiming that the subject property's lease calls for the tenant to pay property taxes. Instead, the lease says, "*Landlord* shall pay, prior to delinquency, all general real estate taxes . . . coming due during the lease term on the Leased Premises. . . ." *Pet'r Ex. 8 at 2 (emphasis added).* While those taxes were relatively insignificant for the tax year ending on May 31, 2006, they were $33,130 for the year ending on May 31, 2007. *Pet'r Exs. 6-7.*

89. But even if the Board were convinced that the Assessor had properly estimated the subject property's net operating income, it would still give little weight to the Assessor's conclusions. In relying on the IAAO paper, the Assessor and Mr. Wuensch used a highly generalized assumption that market rent for the subject property was between 6% and 8% of Restaurant Services' gross sales with little evidence that the assumption applied to the relevant market for the subject property. At most, Mr. Wuensch testified that the owner of Captain D's, a fast-food restaurant in New Castle, told him that fast-food restaurants often lease for 6% of gross sales and that two other appeals from Hancock County and Marion County supported that theory. In fact, the Assessor's own appraiser, Mr. Cecil, testified that he would not consider food sales as relevant if he viewed the property as being owned primarily to produce rent rather than as owner-occupied.

90. Also, the IAAO paper on which Mr. Wuensch and the Assessor rely suggests that a "check" on market rent can be made by taking 12% of a fast-food restaurant's value as estimated under the cost-approach. If one uses the subject property's 2006 assessment, that equals annual rent of $74,280. Using Mr. Allardt's cost-approach estimate of $495,000, the rent would be only $59,000. In either case, that "check" is well below the $ that the Assessor estimated by using 7% of Restaurant Services' gross sales.

91. In finding the income-approach estimates of the Assessor and Mr. Wuensch unpersuasive, the Board does not mean to imply that Restaurant Services' income and expense information was irrelevant. Indeed the Board and the ALJs found otherwise in denying Davis-Gratner's motions to quash and for partial summary judgment and in overruling Davis-Gratner's objection to Respondent's Exhibits 15-17 at the hearing. Both the IAAO paper and testimony at the hearing show that at least some fast-food-restaurant leases are related to the tenant's gross sales. Davis-Gratner's own appraiser, Mr. Allardt, acknowledged as much. Also, a restaurant's sales logically relate, at least partly to things like location and other factors inherent in the real estate out of which the restaurant operates. Thus, while the Board gives little weight to Mr. Wuensch's income-approach analysis that determined economic rent solely by reference to Restaurant Services' gross sales, those sales did at least tend to show that Mr. Semler's market-rent estimate was inadequate.

92. Unfortunately, the parties spent an inordinate amount of time and effort debating whether Restaurant Services' sales and expense information was relevant. And the Assessor's inability to clearly articulate that information's relevance until the day of the hearing contributed to the heart of that dispute. For example, when asked in her deposition where she got the theory that would allow her to determine the subject property's value from the income generated by the KFC restaurant, the Assessor replied "I just made it up." *Pet'r Ex. 3B at 40 of 49*. Even when faced with Davis-Gratner's motion to quash the subpoenas for Restaurant Services' sales and expense information, the Assessor did not

point to the IAAO paper or claim that fast-food-restaurant leases are sometimes based on a percentage of sales.

93. That being said, Davis-Gratner's protests about the relevance of the sales and expense information ring equally hollow. Davis-Gratner claimed that the information was irrelevant because Davis-Gratner was a completely separate entity from Restaurant Services and owned the subject property solely to generate rental income. As already explained, the sales information was at least relevant as a check on the appraisers' various market-rent estimates. Plus, Davis-Gratner's underlying premise—that it used the property solely to generate rent rather than to operate a restaurant—is highly suspect. Davis-Gratner's own actions and evidence belie the purported separation between it and Restaurant Services. The following examples illustrate that point:

- In Davis-Gratner's Form 130 petition, David Granter did not distinguish between the two entities. He listed the predecessor corporation as the property's owner. And he claimed that the subject property was over-assessed because, among other things, "the costs of operating this type of fast food restaurant is increasing at a rate higher than what can be possible [sic] passed on to customers." *Board Ex. A.*

- Davis-Gratner and Restaurant Services did not even file their organizational papers with the Indiana Secretary of State until December 13, 2006, although Ms. Gratner attributed the delay to a miscommunication with counsel.

- Restaurant Services repeatedly adjusted its lease payments to suit the varying needs of both it and Davis-Gratner LLC. For example, it increased its lease payments to cover a corresponding increase in property taxes, even though the lease made Davis-Gratner responsible for those taxes.

- According to Ms. Gratner, she and Joan Davis loaned "the business," which presumably referred to Kentucky Fried Chicken Restaurant Corp., money to pay for remodeling required under its franchise agreement with KFC. *M. Gratner testimony*. Restaurant Services, not Davis-Gratner, operates the restaurant. Restaurant Services therefore presumably succeeded to the corporation's rights and obligations as a franchisee. Yet Davis-Gratner repaid the loan, albeit apparently from increased rental payments.

- Dan Semler, Davis-Gratner's own appraiser, described the subject property as "owner occupied." *Pet'r Ex. 5 at 21*.

94. The Board need not decide whether the line between the two entities was so blurred as to pierce the corporate veil separating them. *See Oliver v. Pinnacle Homes, Inc.*, 769 N.E.2d 1188, 1191 (Ind. Ct. App. 2002) ("Indiana Courts refuse to recognize corporations as separate entities where the facts establish that several corporations are acting as the same entity."). But the Board does find that Davis-Gratner used the subject property as something more like an owner-occupied restaurant than an investment property.

95. Because Restaurant Services' sales and expense information was relevant, the Assessor's pursuit of that information was not "frivolous, unreasonable and groundless" as Davis-Gratner suggests in asking the Board to award it attorney fees for defending against that pursuit. *Petitioner's Post-Trial Brief at 14 n.18*. Thus, even if the Board had the power to award attorney fees—and Davis-Gratner points to no authority to show that it does[10]—the Board would not exercise that power in this case.

[10] Davis-Gratner cites to I.C. § 34-52-1-1, a statute that applies to awarding attorney fees in civil actions, not administrative actions.

### 2. Mr. Cecil's opinion

96. The Board finds Mr. Cecil's valuation opinion similarly unpersuasive. The problems with Mr. Cecil's analysis and underlying judgments are so numerous and profound that they make his ultimate valuation opinion largely unreliable.

97. In his cost-approach analysis, Mr. Cecil estimated the restaurant building's depreciation using an economic life of 60 years, which is 30 years more than Marshall Valuation Service gives for a class-C fast-food restaurant of 'good" construction, and 25 years more than it gives for one of "very good" construction. *Pet'r Ex. 17*. And despite his very limited inspection of the subject property, Mr. Cecil estimated an effective age of only 6 years for a building constructed in 1967. Yet on cross-examination, Mr. Cecil admitted that he did not know how old any of the building's major components were.

98. Granted, the building has been updated over the years and it was remodeled as recently as 2004. But nobody, much less Mr. Cecil, described what that remodeling entailed. At most, Ms. Gratner testified that the remodeling was required by the KFC franchise agreement. Similarly, while the subject property's record card lists the building's effective year of construction as 1995, there is nothing to show who made that judgment or on what it was based. And that effective age does not comply with the Guidelines, which provide an effective age of 29 years for a 38-year-old building in good condition. *Allardt testimony*; REAL PROPERTY ASSESSMENT GUIDELINES FOR 2002 – VERSION A, App. F, at 24 Table F-2.[11]

99. Mr. Cecil's extreme, unsupported estimates for the building's economic life and effective age greatly affected his value conclusions under the cost approach; they led him to estimate physical depreciation of only 10% as compared to the 57% and 70% estimated by Messrs. Semler and Allardt. Mr. Cecil then exacerbated his already woefully

[11] Perhaps the property record card's reference to the building's "effective year" of construction was intended as a weighted calculation of the building's actual age taking into account more recent additions. *See generally*, GUIDELINES, App. F at 5 (describing how to calculate a commercial building's weighted age). Even if that is true, the record lacks any evidence to show on what that calculation was based.

inadequate depreciation estimate by failing to recognize any functional obsolescence. But Mr. Allardt, who had far more experience appraising fast-food restaurants than Mr. Cecil, persuasively explained the inefficiencies of the subject building's design and placement on the lot, which made it more difficult to monitor the dining room and left inadequate stacking room for the restaurant's drive-through window. Thus, the building had at least some functional obsolescence.

100. Mr. Cecil's sales-comparison analysis was almost as bad. He recognized the need to avoid using invalid sales, such as non-arm's-length transactions and sales that included personal property in the sale price. He similarly wanted to avoid sales where a leased fee, rather than a fee simple, interest transferred, at least not without considering adjustments. Yet all of his seven sales fell into one of those categories.

101. First, the disclosure form for sale that Mr. Cecil identified as Sale #7 explained that $480,000 of the $820,000 sale price was attributable to personal property. Mr. Cecil, however, used the full $820,000 price in his analysis. That was a significant oversight and it speaks to the care with which Mr. Cecil performed his appraisal. Plus, sale #7 was one of the four sales that Mr. Cecil ultimately relied on, so the error significantly affected his valuation conclusion.

102. Second, the disclosure statements for two of Mr. Cecil's sales list the same addresses for the buyer and seller. While that does not necessarily show that the parties were related, the Board agrees with Mr. Allardt that it at least raises a red flag as to whether the transactions were at arm's length. Mr. Cecil's general testimony that he checked with assessors to make sure that all his sales were valid does little to assuage that concern.

103. Third, Mr. Allardt convincingly testified that six of Mr. Cecil's seven comparable sales were likely sale-leaseback transactions. Thus, each sale price represented the value of the leased fee interest in the comparable property while Mr. Cecil was valuing the fee simple interest in the subject property. Without more, the Board might not view that as a fatal flaw. But Mr. Allardt explained that sale-leaseback transactions are often financing

arrangements in which multiple properties are bundled together and sale prices are arbitrarily assigned to individual properties. Plus, the overall sale price is often predicated on the value of things in addition to real estate, such as equipment and business enterprise value. Given those dangers, Mr. Cecil's use of those six sales without knowing anything about their particular circumstances significantly detracts from his opinion's reliability.

104. The Assessor, however, argues that deducting enterprise value from a sale price is a controversial theory without a uniform, recognized methodology and that sale-leasebacks of other fast-food restaurants not only can, but must, be considered in valuing the subject property. For support, she cites to *AEI Net Lease Income & Growth Fund v. Erie County Bd. of Revision*, 119 Ohio St. 3d 563, 895 N.E.2d 830 (2008). In that case, the Ohio Supreme court rejected a taxpayer's claim that the amount for which it bought a property should not be considered because the previous owner had bought the property from a restaurant-chain operator in a sale-leaseback transaction and the price that the taxpayer paid was based on the lease payments from that earlier transaction. 895 N.E.2d at 831-32. The court, however, found that the sale-leaseback had been an arm's-length transaction. While the court acknowledged that it had previously expressed concern about using sale-leasebacks in valuing real estate, that concern stemmed from the danger that parties to those transactions might collude to depress a property's value for taxation purposes. *Id*. at 567. That was not the case in the transaction at issue. *Id*. The court also found nothing to support the proposition that the seller had failed to expose the property to whatever markets existed for sale-leasebacks. *Id*. at 835. The court similarly rejected the taxpayer's characterization of the sale-leaseback at issue as a financing transaction. Under the circumstances presented, the court found no evidence that repayment for financing comprised a value separable from the realty. *Id*. at 569-70. For support, it pointed to the property's lease, which recited that it was a true lease and not a financing transaction. *Id*. at 570.

105. Of course, the Assessor does not cite to cases reaching the opposite conclusion. *See e.g. Walgreen Co. v. City of Madison*, 311 Wis. 2d 158, 752 N.W.2d 687, 206 (Wisc. S.Ct.

2008) (explaining that an above-market lease never increases the market value of property rights to a fee simple estate and holding that taxing authority should not have valued property using above-market contract rent), *Beneficial Facilities Corp. v Peapack & Gladstone Borough*, 11 N.J. Tax 359, 376 (1990) (rejecting sale as evidence of a unique office complex's value because it was a sale-leaseback transaction and syndication of partnership interests where the price paid related to the annual rental and income tax benefits, not necessarily to the property's market value). The Assessor also ignores an important part of the IAAO paper on which she otherwise places such great weight. That paper emphasizes that enterprise and other non-real-estate components of value must not be included in a property tax appraisal:

> For property tax purposes, the market value of the fee simple interest under typical market forces or conditions is what is being appraised. It should be kept distinct from the leased fee interest, value in use, or business enterprise appraisal. The appraiser must recognize that there are three elements to a successful restaurant: 1) the real estate; 2) furniture, fixtures, and equipment; and 3) enterprise value. The real estate component is more difficult to value than other real estate because it is inextricably tied to the other two components. . .
>
> While this interpretation does not suggest that the only way to estimate the value of a fast food restaurant is to use sales of closed operations, it compels the appraiser/assessor to do additional research into transactions, leases, and such to find if there is a value enhancement as a result of going concern value.

*Resp't Ex. 8 at 3*.

106. Moreover, the Assessor misses a fundamental distinction between *AEI* and the issue at hand. The *AEI* court addressed the question of whether a specific property's sale price, which was based on lease payments from an earlier sale-leaseback transaction, was a valid measure of its market value. Here, Mr. Cecil sought to compare the subject property—which all the appraisers viewed as owner-occupied and which none of the appraisers recognized as having net operating income of more than $ —to properties that sold in sale-leaseback transactions for prices that were apparently predicated on leases with much higher rent. Mr. Cecil's six sale-leaseback comparables sold for prices ranging from $893,855 to $1,873,000. Using Mr. Cecil's own 7.5%

capitalization rate, the net rent for those properties ranged from $67,039 to $140,475. Thus, even if one agrees with the Assessor's position that a sale-leaseback necessarily shows a property's market value-in-use, the properties that transferred through sale-leasebacks in this case were not comparable to the subject property. At a minimum, Mr. Cecil should have adjusted their sale prices. Indeed, Mr. Cecil himself admitted that he might have looked at adjusting those sale prices if he were to discover that they came from sale-leasebacks.

107. Given the substantial problems with Mr. Cecil's cost and sales-comparison analyses, the Board gives his valuation opinion little weight.

**3. Mr. Semler's opinion**

108. The Board has similar misgivings about Mr. Semler's valuation opinion. For example, in his cost-approach analysis, Mr. Semler used the Marshall Valuation Service data for general restaurant buildings rather than for fast-food restaurants. And, while Mr. Semler found that the subject building did not suffer from functional obsolescence for its current use as a fast-food restaurant, he deducted for obsolescence that he attributed to the likelihood that any other use would require a buyer to change the building's appearance or floor plan. That approach ignores Indiana's market value-in-use standard, which focuses on the market value of a property for its current use. *See* MANUAL at 2.

109. But the problem with Mr. Semler's appraisal that most profoundly affected his ultimate valuation opinion was his estimate of the subject property's market rent. Mr. Semler estimated annual market rent of only $7.50 per square foot of building area. That is significantly less than the $14.00-to-$18.00-per-square-foot general range estimated by the other two appraisers. And while Restaurant Services' gross sales may not be dispositive of the subject property's market rent, they at least tend to show that Mr. Semler's estimate was inadequate. That estimate, however, led Mr. Semler to conclude that the restaurant building was valueless, which in turn led to his opinion that the subject property was worth only the value of its land less the cost of razing the building.

### 4. Mr. Allardt's opinion

110. In the end, the Board gives the greatest weight to Mr. Allardt's opinion that the subject property was worth $480,000 as of January 1, 2005, and $487,200 as of January 1, 2006.

111. Of course, as the Assessor points out, Mr. Allardt's opinion also had problems. Unlike Messrs. Cecil and Semler, Mr. Allardt did not prepare a written appraisal report. Although Mr. Allardt testified that USPAP permitted him to give an oral opinion, his testimony in some instances lacked the specificity contained in the other two appraisers' reports. For example, Mr. Allardt gave few details about how he adjusted the sale prices of his comparable properties under his sales-comparison analysis. On the other hand, neither Mr. Semler nor Mr. Cecil provided significantly more detail about the adjustments in their sales-comparison analysis. True, they identified the amounts of their various adjustments, but they said little, if anything about how they quantified those amounts. And in analyzing the other experts' opinions, Mr. Allardt offered additional insight into his own opinion. Thus, while less detailed than it could have been, Mr. Allardt's opinion was not conclusory.

112. The Assessor, however, wrongly claims that Mr. Allardt valued the subject property as something other than a fast-food restaurant. According to the Assessor, by testifying that sale-leaseback transactions often involve amounts attributable to business enterprise value, Mr. Allardt tried to dissuade the Board from relying on other fast-food restaurant sales. *Assessor's Post-Hearing Brief at 17*. Yet for his own sales-comparison analysis, Mr. Allardt used sales of two fast-food restaurants that sold roast beef and an office building that was remodeled for use as a Subway restaurant. Similarly, for his cost-approach analysis, Mr. Allardt used cost information for fast-food restaurants.

112. Finally, the Board does perceive one potential problem with Mr. Allardt's testimony that the Assessor did not highlight. Mr. Allardt testified that he settled on net operating income between $14 and $15 per square foot and that he applied a capitalization rate

close to 9.5%. But those numbers lead to a slightly higher value than he testified to. For example, using rent of $14 per square foot and a 9.5% capitalization rate yields a value of $524,337 ($14/sq.ft. x 3558 square feet ÷ .075 = $524,337). Mr. Allardt, by contrast, settled on a value $495,000. If Mr. Allardt had either prepared a written report or testified in more detail, the reason for that discrepancy might have become clear. In any event, the discrepancy is relatively minor and does not alter the Board's finding that Mr. Allardt's valuation opinion is generally reliable.

113. In sum, while Mr. Allardt's opinion was imperfect, the Board finds it persuasive. Mr. Allardt was by far the most experienced appraiser in valuing both commercial properties generally and fast-food restaurants specifically. His testimony about the generational evolution of how those restaurants were constructed to take advantage of drive-through lanes and about the sale-leaseback market showed his superior knowledge. And, as already explained, his detailed review of the other experts' opinions offered additional insight into, and support for, his own opinion.

## Conclusion

114. Thus, the Board finds that the subject property's assessments do not accurately reflect its market value in use, which was $480,000 as of January 1, 2005, and $487,200 as of January 1, 2006. The property's March 1, 2006, assessment should therefore be changed to $480,000 and its and March 1, 2007, assessment should be changed to $487,200.

## Summary of Final Determination

The Final Determination of the above captioned matter is issued by the Indiana Board of Tax Review on the date first written above.

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Commissioner, Indiana Board of Tax Review

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Commissioner, Indiana Board of Tax Review

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Commissioner, Indiana Board of Tax Review

# IMPORTANT NOTICE

- Appeal Rights -

You may petition for judicial review of this final determination under the provisions of Indiana Code § 6-1.1-15-5, as amended effective July 1, 2007, by P.L. 219-2007, and the Indiana Tax Court's rules. To initiate a proceeding for judicial review you must take the action required within forty-five (45) days of the date of this notice. The Indiana Tax Court Rules are available on the Internet at <http://www.in.gov/judiciary/rules/tax/index.html>. The Indiana Code is available on the Internet at <http://www.in.gov/legislative/ic/code>. P.L. 219-2007 (SEA 287) is available on the Internet at <http://www.in.gov/legislative/bills/2007/SE/SE0287.1.html>