

**STATE OF INDIANA
Board of Tax Review**

FEDERATED DEPARTMENT STORES INC.)	On Appeal from the Marion County Board of Review
)	
Petitioner,)	
)	Petition for Review of Assessment, Form 131
v.)	Petition No. 49-700-95-1-4-00232
)	Parcel No. 7034274
MARION COUNTY BOARD OF REVIEW and WARREN TOWNSHIP ASSESSOR)	
)	
)	
Respondents.)	

Findings of Fact and Conclusions of Law

On January 1, 2002, pursuant to Public Law 198-2001, the Indiana Board of Tax Review (IBTR) assumed jurisdiction of all appeals then pending with the State Board of Tax Commissioners (SBTC), or the Appeals Division of the State Board of Tax Commissioners (Appeals Division). For convenience of reference, each entity (the IBTR, SBTC, and Appeals Division) is hereafter, without distinction, referred to as "State". The State having reviewed the facts and evidence, and having considered the issues, now finds and concludes the following:

Issues

1. Whether the assigned grade factor is correct.
2. Whether economic obsolescence for the subject property is warranted.
3. Whether a rooftop mechanical screen is correctly priced.

Findings of Fact

1. If appropriate, any finding of fact made herein shall also be considered a conclusion of law. Also if appropriate, any conclusion of law made herein shall also be considered a finding of fact.

2. Pursuant to IC 6-1.1-15-3, Danny S. Brown, Director of Property Tax for Federated Department Stores, Inc. (Petitioner) filed a Form 131 petition requesting a review by the State. The Form 131 petition was filed February 20, 1997. The Marion County Board of Review (County Board) Assessment Determination on the underlying Form 130 petition is dated January 24, 1997.

3. Pursuant to IC 6-1.1-15-4, a hearing was held on October 25, 2000 before Hearing Officer Debra Eads. Testimony and exhibits were received into evidence. Mr. Danny Brown and Mr. Scott Brown represented the Petitioner. Mr. William Birkle represented Warren Township. No one appeared to represent Marion County.

4. At the hearing the subject Form 131 petition was made a part of the record and labeled as State Exhibit A. The Form 117 Notice of Hearing on Petition was labeled State Exhibit B. In addition, the following exhibits were submitted to the State:

Petitioner's Exhibit 1 – Brief including (a) discussion of the basis for economic obsolescence; (b) page 32, 50 IAC 2.2-10, (c) Department Store Lease Analysis; (d) sales volume from 1990 thru 1994; (e) Investment Bulletin no. 1300 dated July 13, 1995; (f) survey of mortgage commitments on commercial properties; (g) Petitioner's calculation of economic obsolescence; (h) 1989 State's final determination for the subject property; (i) Petitioner's revision of true tax and assessed values; (j) property record card (PRC) for subject property

Petitioner Exhibit 2 – Volume per sq. ft. for Washington Square store from 1990 thru 1999

Petitioner Exhibit 3 – Information from “Dollars and Cents of Shopping Centers” including analysis of median sales

Petitioner Exhibit 4 – Spreadsheet of Ohio Department Store Leases

The Township representative (Respondent) submitted no written evidence at the hearing.

5. The subject property is a Lazarus department store located at 10202 E. Washington Street, Indianapolis, Warren Township, Marion County.
6. The Hearing Officer did not conduct an on-site inspection of the subject property.

Issue No. 1 - Whether the assigned grade factor is correct.

Issue No. 3 - Whether a rooftop mechanical screen is correctly priced.

7. At the hearing, Mr. Brown withdrew these issues from review by the State. Mr. Brown signed a Withdrawal Agreement to this effect. *State Exhibit C.*

Issue No. 2 – Whether economic obsolescence for the subject property is warranted.

8. The Petitioner contends that the subject property suffers from economic obsolescence due to a decrease in the population for the effective trading area for the subject. A 1995 examination by the Simon Debartolo Group illustrated that the Castleton, Greenwood and Keystone at the Crossing shopping centers realized superior gross sales figures when compared to the subject property. *D. Brown testimony and Petitioner’s Exhibit 1.*

9. In quantifying the obsolescence, the Petitioner referred to a chart in the brief detailing the *projected* sales per square foot for the first five (5) years of operation compared to the Consumer Price Index for the same time period. The actual gross sales for 1994 were compared with the Consumer Price Index for the same year in an attempt to correlate the first five (5) years of operation with the year preceding the 1995 assessment date (year under appeal). The average gross sales for the subject property were compared with average gross sales for all suburban Lazarus shopping center stores, Indiana Lazarus stores and Lazarus stores in Ohio, Indiana and Kentucky. The calculation of economic obsolescence results in a requested economic obsolescence in the amount of \$ 1,200,000. This calculation utilizes a capitalization rate of 10% and a rental amount based on 3% of the economic sales. *D. Brown testimony and Petitioner's Exhibits 1 and 4.*
10. Mr. Scott Brown testified that his employer prior to Federated Department Stores was May Company and their L. S. Ayres store located at Washington Square Mall suffered a low performance commensurate with the subject property.
11. Respondent argued that an obsolescence problem does exist at the Washington Square Mall. The Petitioner's use of sales per square foot requires an examination of the products placed on the sale floor; if products are not available then sales could not be made. *Birkle testimony.*
12. Upon request, the Hearing Officer granted Mr. Birkle additional time to review the Petitioner's evidence and to submit a response. The Hearing Officer also granted the Petitioner's representatives additional time to respond to Mr. Birkle's review of the Petitioner's evidence. The parties were given until November 6 and November 16, 2000 respectively to respond. The Hearing Officer did not receive any response from Mr. Birkle regarding the evidence submitted by the Petitioner and thus no response was forthcoming from the Petitioner. The Requests for Additional Evidence are entered into the record and labeled as State Exhibits D and D1 respectively.

Conclusions of Law

1. The Petitioner is limited to the issues raised on the Form 130 petition filed with the County Board or issues that are raised as a result of the County Board's action on the Form 130 petition. 50 IAC 17-5-3. See also the Forms 130 and 131 petitions authorized under Ind. Code §§ 6-1.1-15-1, -2.1, and -4. In addition, Indiana courts have long recognized the principle of exhaustion of administrative remedies and have insisted that every designated administrative step of the review process be completed. *State v. Sproles*, 672 N.E. 2d 1353 (Ind. 1996); *County Board of Review of Assessments for Lake County v. Kranz* (1964), 224 Ind. 358, 66 N.E. 2d 896. Regarding the Form 130/131 process, the levels of review are clearly outlined by statute. First, the Form 130 petition is filed with the County and acted upon by the County Board. Ind. Code §§ 6-1.1-15-1 and -2.1. If the taxpayer, township assessor, or certain members of the County Board disagree with the County Board's decision on the Form 130, then a Form 131 petition may be filed with the State. Ind. Code § 6-1.1-15-3. Form 131 petitioners who raise new issues at the State level of appeal circumvent review of the issues by the County Board and, thus, do not follow the prescribed statutory scheme required by the statutes and case law. Once an appeal is filed with the State, however, the State has the discretion to address issues not raised on the Form 131 petition. *Joyce Sportswear Co. v. State Board of Tax Commissioners*, 684 N.E. 2d 1189, 1191 (Ind. Tax 1997). In this appeal, such discretion will not be exercised and the Petitioner is limited to the issues raised on the Form 131 petition filed with the State.

2. The State is the proper body to hear an appeal of the action of the County pursuant to Ind. Code § 6-1.1-15-3.

Indiana's Property Tax System

3. Indiana's real estate property tax system is a mass assessment system. Like all other mass assessment systems, issues of time and cost preclude the use of assessment-quality evidence in every case.
4. The true tax value assessed against the property is not exclusively or necessarily identical to fair market value. *State Board of Tax Commissioners v. Town of St. John*, 702 N.E. 2d 1034, 1038 (Ind. 1998)(*Town of St. John V*).
5. The Property Taxation Clause of the Indiana Constitution, Ind. Const. Art. X, § 1 (a), requires the State to create a uniform, equal, and just system of assessment. The Clause does not create a personal, substantive right of uniformity and equality and does not require absolute and precise exactitude as to the uniformity and equality of each *individual* assessment. *Town of St. John V*, 702 N.E. 2d at 1039 – 40.
6. Individual taxpayers must have a reasonable opportunity to challenge their assessments. But the Property Taxation Clause does not mandate the consideration of whatever evidence of property wealth any given taxpayer deems relevant. *Id.* Rather, the proper inquiry in all tax appeals is “whether the system prescribed by statute and regulations was properly applied to individual assessments.” *Id.* at 1040. Only evidence relevant to this inquiry is pertinent to the State's decision.

Burden

7. Ind. Code § 6-1.1-15-3 requires the State to review the actions of the County Board, but does not require the State to review the initial assessment or undertake reassessment of the property. The State has the ability to decide the administrative appeal based upon the evidence presented and to limit its review to the issues the taxpayer presents. *Whitley Products, Inc. v. State Board of Tax Commissioners*, 704 N.E. 2d 1113, 1118 (Ind. Tax 1998) (citing *North Park*

Cinemas, Inc. v. State Board of Tax Commissioners, 689 N.E. 2d 765, 769 (Ind. Tax 1997)).

8. In reviewing the actions of the County Board, the State is entitled to presume that its actions are correct. “Indeed, if administrative agencies were not entitled to presume that the actions of other administrative agencies were in accordance with Indiana law, there would be a wasteful duplication of effort in the work assigned to agencies.” *Bell v. State Board of Tax Commissioners*, 651 N.E. 2d 816, 820 (Ind. Tax 1995). The taxpayer must overcome that presumption of correctness to prevail in the appeal.
9. It is a fundamental principle of administrative law that the burden of proof is on the person petitioning the agency for relief. 2 Charles H. Koch, Jr., *Administrative Law and Practice*, § 5.51; 73 C.J.S. Public Administrative Law and Procedure, § 128.
10. Taxpayers are expected to make factual presentations to the State regarding alleged errors in assessment. *Whitley*, 704 N.E. 2d at 1119. These presentations should both outline the alleged errors and support the allegations with evidence. “Allegations, unsupported by factual evidence, remain mere allegations.” *Id* (citing *Herb v. State Board of Tax Commissioners*, 656 N.E. 2d 890, 893 (Ind. Tax 1995)). The State is not required to give weight to evidence that is not probative of the errors the taxpayer alleges. *Whitley*, 704 N.E. 2d at 1119 (citing *Clark v. State Board of Tax Commissioners*, 694 N.E. 2d 1230, 1239, n. 13 (Ind. Tax 1998)).
11. One manner for the taxpayer to meet its burden in the State’s administrative proceedings is to: (1) the taxpayer must identify properties that are similarly situated to the contested property, and (2) establish disparate treatment between the contested property and other similarly situated properties. *Zakutansky v. State Board of Tax Commissioners*, 691 N.E. 2d 1365, 1370 (Ind. Tax 1998). In this way, the taxpayer properly frames the inquiry as to “whether the system

prescribed by statute and regulations was properly applied to individual assessments.” *Town of St. John V*, 702 N.E. 2d at 1040.

12. The taxpayer is required to meet his burden of proof at the State administrative level for two reasons. First, the State is an impartial adjudicator, and relieving the taxpayer of his burden of proof would place the State in the untenable position of making the taxpayer’s case for him. Second, requiring the taxpayer to meet his burden in the administrative adjudication conserves resources.
13. To meet his burden, the taxpayer must present probative evidence in order to make a prima facie case. In order to establish a prima facie case, the taxpayer must introduce evidence “sufficient to establish a given fact and which if not contradicted will remain sufficient.” *Clark*, 694 N.E. 2d at 1233; *GTE North, Inc. v. State Board of Tax Commissioners*, 634 N.E. 2d 882, 887 (Ind. Tax 1994).
14. In the event a taxpayer sustains his burden, the burden then shifts to the local taxing officials to rebut the taxpayer’s evidence and justify its decision with substantial evidence. 2 Charles H. Koch, Jr. at §5.1; 73 C.J.S. at § 128. See *Whitley*, 704 N.E. 2d at 1119 (The substantial evidence requirement for a taxpayer challenging a State Board determination at the Tax Court level is not “triggered” if the taxpayer does not present any probative evidence concerning the error raised. Accordingly, the Tax Court will not reverse the State’s final determination merely because the taxpayer demonstrates flaws in it).

Review of Assessments After *Town of St. John V*

15. Because true tax value is not necessarily identical to market value, any tax appeal that seeks a reduction in assessed value solely because the assessed value assigned to the property does not equal the property’s market value will fail.

16. Although the Courts have declared the cost tables and certain subjective elements of the State's regulations constitutionally infirm, the assessment and appeals process continue under the existing rules until a new property tax system is operative. *Town of St. John V*, 702 N.E. 2d at 1043; *Whitley*, 704 N.E. 2d at 1121.

Issues 1 and 3 - Grade Factor and Rooftop Mechanical Screen Pricing

17. At the hearing, the Petitioner withdrew these issues from review by the State. Mr. Brown signed a Withdrawal Agreement to this effect (State Exhibit C). No change in the assessment is made as a result of these withdrawals.

Issue 2 - Economic Obsolescence

18. Depreciation is an essential element in the cost approach to valuing property. Depreciation is the loss in value from any cause except depletion, and includes physical depreciation and functional and external (economic) obsolescence. International Association of Assessing Officials (IAAO) Property Assessment Valuation, 153 & 154 (2nd ed. 1996); *Canal Square Limited Partnership v. State Board of Tax Commissioners*, 694 N.E. 2d 801, 806 (Ind. Tax 1998)(citing Am. Inst. of Real Estate Appraisers, *The Appraisal of Real Estate* (10th ed. 1992)).
19. Depreciation is a concept in which an estimate must be predicated upon a comprehensive understanding of the nature, components, and theory of depreciation, as well as practical concepts for estimating the extent of it in improvements being valued. 50 IAC 2.2-10-7.
20. Depreciation is a market value concept and the true measure of depreciation is the effect on marketability and sales price. IAAO Property Assessment Valuation at 153. The definition of obsolescence in the Regulation, 50 IAC 2.2-10-7, is tied to the one applied by professional appraisers under the cost approach. *Canal*

Square, 694 N.E. 2d at 806. Accordingly, depreciation can be documented by using recognized appraisal techniques. *Id.*

21. Functional obsolescence is a loss of value in a property improvement due to changes in style, taste, technology, needs and demands. Functional obsolescence exists where a property suffers poor or inappropriate architecture, lack of modern equipment, wasteful floor plans, inappropriate room sizes, inadequate heating or cooling capacity and so on. It is the inability of a structure to perform adequately the function for which it is currently used. IAAO Property Assessment Valuation at 154 & 155.
22. External or economic obsolescence is the loss in value as a result of an impairment in utility and desirability caused by factors external to the property (for example, national economic conditions). IAAO Property Assessment Valuation at 155.
23. The elements of functional and economic obsolescence can be documented using recognized appraisal techniques. These standardized techniques enable a knowledgeable person to associate cause and effect to value pertaining to a specific property. *Canal Square*, 694 N.E. 2d 801.
24. There are five (5) recognized methods used to measure depreciation, including obsolescence; namely: (1) sales comparison method, (2) the capitalization of income method, (3) the economic age-life method, (4) the modified economic age-life method, and (5) the observed condition method.
25. Of the five (5) recognized methods two (2) are indirect and three (3) are direct methods. Direct methods involve measuring the depreciation of the subject property, whereas indirect methods use sales of comparable properties and income loss from rental properties to measure depreciation. The methods are categorized as follows:

Indirect methods:

1. sales comparison method
2. capitalization of income method

Direct Methods:

1. economic age-life method
2. modified economic age-life method
3. observed condition (breakdown) method

IAAO Property Assessment Valuation, 155-156 (2nd ed. 1996)

Burden regarding the obsolescence claim

26. “[I]n advocating for an obsolescence adjustment, a taxpayer must first provide the State Board with probative evidence sufficient to establish a prima facie case as to the causes of obsolescence.” *Champlin Realty Company v. State Board of Tax Commissioners*, 745 N.E. 2d 928, 932 (Ind. Tax 2001).
27. The identification of causes of obsolescence requires more than randomly naming factors. “Rather, the taxpayer must explain how the purported causes of obsolescence cause the subject improvements to suffer losses in value.” *Champlin*, 745 N.E. 2d at 936.
28. “Without a loss of value, there can be no economic obsolescence.” *Pedcor v. State Board of Tax Commissioners*, 715 N.E. 2d 432, 438 (Ind. Tax 1999).
29. It is incumbent on the taxpayer to establish a link between the evidence and the loss of value due to obsolescence. After all, the taxpayer is the one who best knows his business and it is the taxpayer who seeks to have the assessed value of his property reduced. *Rotation Products Corp. v. Department of State Revenue*, 690 N.E. 2d 795, 798 (Ind. Tax 1998).

30. Regarding obsolescence, the taxpayer has a two-prong burden of proof: (1) the taxpayer has to prove that obsolescence exists, and (2) the taxpayer must quantify it. *Clark v. State Board of Tax Commissioners*, 694 N.E. 2d 1230, 1233 (Ind. Tax 1998).

Evidence submitted

32. It is the Petitioner's opinion that economic obsolescence is present as a result of negative external influences. The Petitioner submits what it characterizes as an "economic income approach" calculation (Petitioner's Exhibit 1), resulting in an obsolescence figure of \$1,200,100, along with a 1989 State determination for the subject property.
33. Before applying the evidence to reduce the contested assessment, the State must first analyze the reliability and probity of the evidence to determine what, if any, weight to accord it.
34. It should first be noted, that at the hearing Mr. Birkle stated that an obsolescence problem does exist at the Washington Square Mall (where subject structure is located) but Mr. Birkle did not indicate the amount of obsolescence that should be applied. Due to the fact that the parties to this appeal agree that obsolescence does exist, the first part of the Petitioner's burden has been met. Having said that, it is now the Petitioner's burden to quantify the amount of obsolescence they seek.

Analysis of Evidence Submitted

35. Capitalization is the process of converting a series of anticipated future payments (income) into present value. Capitalization transforms net operating income produced by a property into a *property value*. The capitalization process restates market value by converting the future benefits of property ownership into an expression of present worth. IAAO Property Assessment Valuation at 229.

36. In the income approach, accrued depreciation is accounted for in the process of estimating the quantity, quality, and duration of the income and, ultimately, the property value. By the capitalization of income method, an estimate of depreciation may be calculated by capitalizing the net income of the subject property into an estimate of value, and deducting the site value. The resulting indicated improvement value is then compared with the estimated cost new to estimate the percentage of improvement value remaining. IAAO Property Assessment Valuation at 159.
37. The basic steps in the income approach are as follows:
- (1) Estimate potential gross income.
 - (2) Deduct for vacancy and collection loss.
 - (3) Add miscellaneous income to get the effective gross income.
 - (4) Determine operating expense.
 - (5) Deduct operating expenses from the effective gross income to determine net operating income before discount, recapture, and taxes.
 - (6) Select the proper capitalization rate.
 - (7) Determine the appropriate capitalization procedure to be used.
 - (8) Capitalize the net operating income into an estimated property value.
38. The Petitioner's "economic income approach" is flawed for the following reasons:
- a. The Petitioner fails to use the income capitalization method properly. The Petitioner's calculation does not attempt to estimate the subject property's value;
 - b. The Petitioner fails to determine the replacement cost new for the structure;
 - c. The calculation fails to make an estimate of depreciation by capitalizing the net income of the property into an estimate of value, and deducting the site value. The resulting improvement value would then be compared to the estimated cost new to estimate the percentage of improvement value

remaining. Such a comparison would indicate the amount of depreciation (accrued) from all sources (physical, obsolescence);

- d. The Petitioner uses an income per square foot of space value (actual income) instead of gross potential income;
 - e. The Petitioner uses the steps associated with the income capitalization method to value as steps to determine the obsolescence value;
 - f. The Petitioner's calculation includes a vacancy allowance but fails to include any losses due to collections;
 - g. The Petitioner did not submit any documentation in support of its purported actual sales and average sales figures; and
 - h. The 10% capitalization rate used by the Petitioner is explained as "that which is commonly experienced in the real estate market for Retail properties in the first quarter of 1995."
39. Of all the flaws addressed within the Petitioner's calculation, the capitalization rate is the most important. Capitalization rates are critical in the valuation process, and must be supported. Small changes in the capitalization rates make significant changes in value. For example, in the case at bar, the Petitioner determined the rent loss to be \$120,071 and divides this amount by the capitalization rate to determine economic obsolescence in the amount of \$1,200,000. However, if the capitalization rate is 11% and using the Petitioner's calculation, the purported economic obsolescence equals \$1,091,554.
40. Because significant differences in values, capitalization rates should never be talked about in generalizations or averages. They are specific to the risk of investment, the duration of the income stream, and the shape of the income stream into the foreseeable future. Therefore, a Petitioner must submit a detailed documentation of the development of its capitalization rate, or, in the alternative document and use the rate of return the company is receiving on "its overall" operation. The Petitioner failed to do this.

41. Also, the Petitioner's calculations use actual sales per square foot of store space and compare this value to "averages" of sales per square foot of store space to other stores owned by the Petitioner. The Petitioner then takes the difference between the subject's actual sales and that of the "averages" and determines an obsolescence value. This determined obsolescence value is then deducted from the reproduction cost of the structure to determine a True Tax Value.
42. The use of this type of comparison or calculation is also incorrect. The Petitioner makes an assumption that True Tax Value and Market Value are synonymous and interchangeable. Such an assumption is incorrect. Ind. Code § 6-1.1-31-6(c) states, "With respect to the assessment of real property, true tax value does not mean fair market value. True tax value is the value determined under the rules of the state board of tax commissioners." In Indiana, tax assessments, for the assessment year at issue, are not required to be based on market value. *Boehm v. State Board of Tax Commissioners*, 675 N.E. 2d 318, 327 (Ind. 1996).
43. In addition, the Petitioner submitted a State determination for 1989 that granted 15% obsolescence to the subject structure. The State will not apply an obsolescence depreciation factor on the basis of its Final Determination for a 1989 appeal. That determination did not specifically state the basis for the application of obsolescence, and did not reflect or meaningfully deal with the evidence considered in determining the 15% factor that was applied. Instead, the Final Determination only said, "Upon careful consideration of the evidence presented and in consideration of 50 IAC 2.1-5-1, it is determined 15% obsolescence is applied to the Lazarus store."
44. In the final analysis of the issue of this appeal, the Petitioner is requesting the application of obsolescence based solely on the fact that the subject store, in Washington Square Mall is not as *profitable* as other stores owned by the Petitioner. The issue is one of *profitability* and not one of obsolescence attributed to the structure.

45. If a business fails to make a profit it is not the job of the State or the purpose of the appeal process to rectify the profitability of a business. It is the Petitioner's burden to show how the subject structure is obsolete and suffers a loss in value.
46. As stated earlier, "Without a loss of value, there can be no economic obsolescence." *Pedcor v. State Board of Tax Commissioners*, 715 N.E. 2d 432, 438 (Ind. Tax 1999). The Petitioner has not shown that the subject property suffers from a loss in value. In fact, the Petitioner makes no statements regarding the value of the subject structure.
47. For all the reasons set forth above, the Petitioner failed to meet the second prong of their burden of proof in this appeal. Accordingly, no change in the assessment is made as a result of this issue.

SUMMARY OF STATE DETERMINATIONS

Issue No. 1 – Grade – Withdrawn by Petitioner

Issue No. 2 – Obsolescence – No change

Issue No. 3 – Rooftop mechanical screen – Withdrawn by Petitioner

The above stated findings and conclusions are issued in conjunction with, and serve as the basis for, the Final Determination in the above captioned matter, both issued by the Indiana Board of Tax Review this ____ day of _____, 2002.

Chairman, Indiana Board of Tax Review

IMPORTANT NOTICE

- APPEAL RIGHTS -

You may petition for judicial review of this final determination pursuant to the provisions of Indiana Code § 6-1.1-15-5. The action shall be taken to the Indiana Tax Court under Indiana Code § 4-21.5-5. To initiate a proceeding for judicial review you must take the action required within forty-five (45) days of the date of this notice.