

STATE OF NORTH CAROLINA

BEFORE THE PROPERTY TAX COMMISSION
SITTING AS THE STATE BOARD
OF EQUALIZATION AND REVIEW

COUNTY OF WAKE

01 PTC 544

IN THE Matter of:

APPEAL OF: **IBM CREDIT CORPORATION**

from the decision of the Durham County Board of
County Commissioners concerning the valuation
of business personal property for tax year 2001.

**FINAL DECISION ON
SECOND REMAND**

This Matter is before the North Carolina Property Tax Commission ("Commission") for reconsideration of the evidence presented in this appeal in accordance with the Opinion dated December 8, 2009 from the North Carolina Court of Appeals. By Order dated March 11, 2010, the North Carolina Supreme Court declined to grant discretionary review. This Matter is thus before the Commission as remanded by the Court of Appeals.

Chairman Wheeler, Vice Chair Plyler and Commissioners Wilmoth, Dixon, and Pittman reconsidered this matter as remanded.

Statement of Case and Facts

This Matter was initially heard before the North Carolina Property Tax Commission ("Commission"), sitting as the State Board of Equalization and Review, in the City of Raleigh, Wake County, North Carolina, during the Commission's regular scheduled session of hearings on October 10-13, 2005 and the Commission's regular scheduled session of hearings on December 15-16, 2005, pursuant to the appeal of IBM Credit Corporation ("IBM Credit") from the decision of the Durham County Board of County Commissioners ("County Board") concerning the valuation of certain business personal property for tax year 2001.

Chairman Wheeler presided over the October 2005 session of hearings with then Vice Chair Cope and Commissioners Wilmoth, Young and former Commissioner Raynor participating.

Chairman Wheeler presided over the December 2005 session of hearings with Commissioners Wilmoth, Young and former Commissioner Raynor participating. The parties agreed to proceed with this session in the absence of then Vice Chair Cope.

After the first Opinion and remand by the Court of Appeals, the Commission heard this matter on briefs and entered a second Final Decision, dated August 29, 2008, which affirmed Durham County's assessment of IBM Credit's computer equipment pursuant to Schedule U5. IBM then appealed again to the Court of Appeals, which has led to this second remand.

The subject of this appeal is Durham County's 2001 assessment of 40,779 separate individual items of computer and computer-related equipment that IBM Credit has on lease to end-users in Durham County. For tax year 2001, the leased equipment falls into four

categories: mainframe computers; mid-range computers; personal computers; and peripheral equipment (printers, scanners, etc.). IBM Credit itself is using none of the equipment. It leases all of the equipment to a variety of customers in Durham County, one of which is IBM Credit's parent corporation.

For tax year 2001, IBM Credit commissioned the services of NACOMEX U.S.A. Inc, ("NACOMEX") to list its computer and computer-related equipment (data processing tangible personal property) with the Durham County Tax Office. Based upon the services of NACOMEX, the total value listed by IBM Credit for the relevant tax year (January 1, 2001) for its data processing tangible personal property was \$96,458,707.00.¹ To assess the value of the 40,779 pieces of computer equipment, Durham County used Schedule U5 of the 2001 Cost Index and Depreciation Schedules published by the North Carolina Department of Revenue ("Department"). Based upon the depreciation tables of Schedule U5, Durham County assessed IBM Credit's equipment at a total value of \$144,277,140.00.²

IBM Credit also presented factual testimony at the 2005 hearings from its experienced management personnel as to the fair market value of its equipment. This evidence included acquisition costs and residual values based on sales of the computer equipment. Most of the equipment is leased by IBM Credit for three years. Ninety-five percent (95%) of the equipment is manufactured by IBM.

IBM Credit brought the appeal to the Commission because of its contention that the assessment by Durham, County violates N.C. Gen. Stat. §§ 105-283, 105-284 and other applicable law in that IBM Credit's property has been assessed at an amount that exceeds its true value in money.³

Durham County initially contended that IBM Credit's equipment had been correctly assessed pursuant to Schedule U5. Based on the Court of Appeals' Opinions and the evidence of record, Durham County on remand contends that the evidence from IBM Credit's management personnel as to the actual value of this equipment and the three-year lease terms should be used to appraise this equipment. Durham County requested that the Commission reopen the record to answer the specific questions contained in the Court of Appeals' Opinion dated December 8, 2009. When IBM Credit objected to any new evidence on remand, and cited caselaw authority, the County agreed to hear this matter on the existing record.

Briefs and proposed orders were filed by the parties in March, 2011. The Commission heard argument of counsel on May 25, 2011.

Evidence

¹ See IBM Credit's Application for Hearing, dated January 25, 2002 and filed with the Commission on January 22, 2002.

² Durham County's 'Exhibit 4 (Durham County's 2001 Business Personal Property Appraisal of IBM Credit's business personal property (by district)).

³ See Attachment A to IBM Credit's Application for Hearing, dated January 25, 2002.

The exhibits and testimony presented by IBM Credit and reconsidered by the Commission on second remand of this matter consists of the following:

- IBM Credit's Exhibit 1 (IBM Credit's 2001 Business Personal Property Tax Listing filed with Durham County).
- IBM Credit's Exhibit 2 (IBM Credit's 2001 Durham County personal property tax bills).
- IBM Credit's Exhibit 3 (Excerpts from IBM Credit's Detailed Listing Printout (by district)).
- IBM Credit's Exhibit 4 (Application for Hearing, Form AV-14 dated January 25, 2002 and attachments A, B, and C).
- IBM Credit's Exhibit 30 (Curriculum Vitae of Robert Zises).
- IBM Credit's Exhibit 31 (Curriculum Vitae of Dennis Neilson).
- IBM Credit's Exhibit 33 (February 15, 2001 NACOMEX Report).
- IBM Credit's Exhibit 37 (Excerpts from the subset of the NACOMEX database utilized in preparation of the February 15, 2001 NACOMEX Report).
- IBM Credit's Exhibit 43 (North Carolina Department of Revenue 2001 Cost Index and Depreciation Schedules (Schedule U5)).
- IBM Credit's Exhibit 44 (Memo to Users of 2001 Cost Index and Depreciation Schedules).
- IBM Credit's Exhibit 61 (Excerpts from Valuing Machinery and Equipment (American Society of Appraisers' Textbook)).
- Oral Testimony of Robert Zises, admitted as an expert in the appraisal of computer equipment.
- Oral Testimony of David B. Baker, North Carolina Department of Revenue, Director, Property Tax Division.
- Oral Testimony of Dennis Neilson (St. Charles, Ill.), called as a rebuttal witness.
- Oral Testimony of Chuck Lally, 10556 Clubmont Road, Raleigh, NC 27617.
- Oral Testimony of Paul Copeland (Gaithersburg, Maryland).
- Oral Testimony of Vincent Palmiotto, 103 Pocono Road, Brookfield, Connecticut.

IBM Credit also provided to the Commission a full copy of the asset listing of its computer equipment showing, among other matters, the dates of acquisition and costs. The exhibits and testimony presented by Durham County and reconsidered by the Commission on second remand of this matter consists of the following:

- Durham County's Exhibit 3 (Durham County's Valuation Methods of Procedures — Excerpts from the North Carolina Department of Revenue, Property Tax Division's 2001 Cost Index and Depreciation. Schedules).
- Durham County's Exhibit 4 (Durham County's 2001 Business Personal Property Appraisal of IBM Credit's business personal property (by district)).
- Durham County's Exhibit 7 (IBM Credit's leases).
- Durham County's Exhibit 8 (Report by BCRI — Valuation Services).

- Oral Testimony of Kenneth L. Joyner, Durham County Assessor, admitted as an expert in the appraisal of property.
- Curriculum Vitae of Kenneth L. Joyner.
- Oral Testimony of Stephen L. Barreca, admitted as an expert in the area of real and personal property appraisal.
- Curriculum Vitae of Stephen L. Barreca.

Commission Documents

- C-1 IBM Credit's Notice of Appeal, filed December 28, 2001.
- C-2 Commission acknowledgment of C-1, dated December 28, 2001.
- C-3 IBM Credit's Application for Hearing, with Attachments A, B, and C, dated January 25, 2002 and filed with the Commission on January 25, 2002.
- C-4 Commission acknowledgment of C-3, dated January 29, 2002.
- C-5 Durham County's First Set of Interrogatories and Request for Production of Documents, filed August 19, 2002.
- C-6 Letter from Taxpayer's attorney to Commission Secretary, filed October 23, 2002.
- C-7 Durham County's Motion to Compel or Dismiss, filed August 8, 2003.
- C-8 Commission acknowledgment of C-7, dated August 13, 2003.
- C-9 Letter to Commission Secretary changing date of hearing, dated August 28, 2003.
- C-10 Response of Taxpayer to County's Motion to Dismiss, filed September 18, 2003.
- C-11 Letter from Taxpayer's attorney to Commission Secretary, filed November 12, 2003.
- C-12 Transmittal letter and Recommendation of Commission Representative, dated February 11, 2004.
- C-13 Transmittal letters and Orders of Commission, dated March 15, 2003.
- C-14 IBM Credit's Motion for Protective Order filed February 3, 2005.
- C-15 Durham County's Response to Motion for Protective Order, filed February 14, 2005.
- C-16 Letter from Durham County to Taxpayer's attorney, faxed March 14, 2005.
- C-17 Letter from Durham County to Taxpayer's attorney, filed March 16, 2005.
- C-18 Letter from Taxpayer's attorney to County Attorney, faxed March 17, 2005.
- C-19 Executed Scheduling Order, filed March 21, 2005.
- C-20 Letter from Taxpayer's Attorney to Durham County, faxed March 16, 2005.
- C-21 Durham County's Response to Taxpayer's Scheduling Order, filed March 21, 2005.
- C-22 Letter from Taxpayer's attorney to County attorney, filed March 18, 2005.
- C-23 Letter from County attorney to Commission, Secretary, filed March 28, 2005.
- C-24 Transmittal letter and Protective Order, dated March 23, 2005.
- C-25 Letter from County attorney to Taxpayer's attorney, filed April 25, 2005.
- C-26 Transmittal letter and Scheduling Order, dated April 18, 2005.

- C-27 Letter from County attorney to Taxpayer's attorney, filed April 21, 2005, (i.e. Sample Lease request).
- C-28 Letter from County attorney to Taxpayer's attorney, filed May 6, 2005.
- C-29 Letter from County attorney to Taxpayer's attorney, filed May 19, 2005.
- C-30 Letter from Taxpayer's attorney to County attorney, faxed May 24, 2005.
- C-31 Letter from County attorney to Taxpayer's attorney, filed June 2, 2005.
- C-32 Letter from County attorney to Taxpayer's attorney, filed June 20, 2005.
- C-33 Letter from County attorney to Taxpayer's attorney, filed June 20, 2005.
- C-34 Letter from County attorney to Taxpayer's attorney, filed July 5, 2005.
- C-35 Letter from County attorney to Commission Secretary, filed July 28, 2005.
- C-36 Proposed hearing calendar for October session of Property Tax Commission, dated August 23, 2005.
- C-37 Joint motion to amend scheduling Order, filed August 23, 2005.
- C-38 Fax from Taxpayer's attorney, dated August 25, 2005.
- C-39 Transmittal letter and amended scheduling Order, dated August 30, 2005.
- C-40 Amended proposed healing calendar, dated August 30, 2005.
- C-41 IBM Credit's supplemental expert witness designation, filed September 21, 2005.
- C-42 Notice of Hearing, dated September 22, 2005.
- C-43 Durham County's Motion In Limine, filed September 22, 2005.
- C-44 Commission acknowledgment of C-43, dated September 27, 2005.
- C-45 Request of Taxpayer's attorney to subpoena David Baker, filed September 29, 2005.
- C-46 Response of Taxpayer's attorney to Durham County's Motion In Limine, filed September 30, 2005.
- C-47 Taxpayer's Pre-Hearing Memorandum, filed September 30, 2005.
- C-48 Durham County's Motion to Disqualify, filed September 30, 2005.
- C-49 Order on Final Pre-Hearing Conference, filed September 30, 2005.
- C-50 Copy of Subpoena, filed October 4, 2005.

In addition to the above-referenced evidence and documents, the Commission considered the following:

- Final Decision of the Property Tax Commission entered on March 30, 2006.
- *In re Appeal of Southern Railway*, 313 N.C. 177, 328 S.E. 2d 235, (1985).
- *In re Appeal of IBM Credit Corporation*, 362 N.C. 228, 657 S.E.2d 355 (2008).
- *In re Appeal of IBM Credit Corporation*, 186 N.C. App 223, 650 S.E.2d 828 (2007) (“IBM Credit I).
- *In re Appeal of IBM Credit Corporation*, ___ N.C. App. ___, 689 S.E.2d 487 (2009) (“IBM Credit II).
- *In re Amp, Inc.*, 287 N.C. 547, 215 S.E.2d 752 (1975).
- The parties briefs, proposed orders and arguments on the second remand.

Burden of Proof

Ad valorem assessments by a county are presumed to be correct. The Court of Appeals ruled that Durham County produced sufficient evidence “to establish a presumption of correctness.” *IBM Credit II*, 689 S.E.2d at 489-90. The Court of Appeals further ruled that IBM Credit presented evidence “tending to show” that Durham County used an “arbitrary method of valuation.” The burden is now shifted to Durham County, the taxing authority, to show “that the methods used do in fact produce ‘true value.’” *IBM Credit II*, 689 S.E.2d at 491.

Specifically, the Court of Appeals gave the following direction as to the remand to the Commission:

We therefore reverse the Final Decision of the Commission, and again remand to the Commission for a reasoned decision with regard to what amount of depreciation deduction should have been deducted from the valuation to account for functional and economic obsolescence due to market conditions.

IBM Credit II at 494.

The record is not sufficient for the County or this Commission to address the issues raised by the Court of Appeals on remand and to show that applicable Schedule U5 produces “true value.” IBM Credit has opposed the Commission’s taking new evidence. Also, the Commission has twice ruled that the NACOMEX Report is not credible or reliable, and such rulings have not been overturned on appeal. Therefore, the Commission will determine the true value of IBM Credit’s property based on the remaining evidence in the record. In so doing, the Commission will be guided by the six issues raised by the Court of Appeals in *IBM Credit II*. *Id.* at 491-93.

The following findings are made in accordance with the Court of Appeals’ two Opinions, and made after considering and weighing all evidence of record, the parties’ briefs on remand and oral argument. Based on the greater weight of the evidence of record and relying primarily on the factual testimony of IBM Credit’s management personnel and IBM Credit’s exhibits, the Property Tax Commission makes the following Findings of Fact.

Findings of Fact

1. IBM Credit is a corporation engaged in the business of leasing computer and computer-related equipment. As of the relevant tax date (January 1, 2001), the leased equipment under appeal falls within four categories: mainframe computers; mid-range computers; personal computers; and peripheral devices, such as printers, scanners and storage devices.

2. As of January 1, 2001, IBM Credit leased the 40,779 pieces of computer and computer-related equipment to 364 customers in Durham County. With respect to the 364 customers, the leasing process was structured so that the IBM Credit customer would

negotiate an acquisition price for a particular item with a vendor. IBM Credit would then purchase the item at the price negotiated between the customer and the vendor. After acquiring the computer equipment, IBM Credit would in turn lease it to the customer, typically for a term of three years, in exchange for monthly payments. IBM Credit would retain whatever residual value the computer equipment and computer-related equipment retained at the end of the lease term.

3. IBM Credit duly and timely filed its business personal property listings with the Durham County Tax Office ("Tax Office") for tax year 2001.⁴ IBM Credit retained the services of NACOMEX U.S.A. Inc.⁵ to assist in listing its computer and computer-related equipment in Durham County. NACOMEX U.S.A. Inc. did not conduct an asset-by-asset inventory of the equipment but did rely on descriptions provided on IBM Credit's asset list and assumed that all of the equipment valued is maintained in a good and serviceable manner.⁶

4. To determine the value of the 40,779 pieces of computer and computer-related equipment for tax year 2001, Durham County used the 2001 Cost index and Depreciation Schedules ("Schedule U5") developed and published by the North Carolina Department of Revenue ("Department"). The Department developed Schedule U5 to assist county tax assessors in determining the assessed value of computer and computer-related equipment.⁷ Based upon the depreciation tables of Schedule U5, Durham County assessed IBM Credit's computer and computer-related equipment at a total value of \$144,277,140.00.⁸ To arrive at this total value, Durham County used IBM Credit's listing and applied the Schedule U5. In particular, Durham County used the original cost listed by IBM Credit on its business personal property listing by year for the computer and computer-related equipment and then applied Schedule U5 to arrive at the final value for each listing.⁹

5. IBM Credit challenged Durham County's assessment of its computer and computer-related equipment by filing an appeal with the County Board. After the County Board denied IBM Credit's request to utilize additional depreciation for its computer and computer-related equipment for tax year 2001,¹⁰ IBM Credit filed an appeal with the

⁴ IBM Credit's Exhibit 1, 2001 Business Personal Property Tax Listing filed with Durham County.

⁵ NACOMEX U.S.A. Inc. is a computer broker that created the NACOMEX Database.

⁶ IBM Credit's Exhibit 33 (February 15, 2001 NACOMEX Report).

⁷ The Department revised Schedule U5 after the Commission's ruling in *In re Appeal of Northern Telecom, Inc.*, 91 PTC 26, 92 PTC 413, 93 PTC 23 (1994).

⁸ Durham County's Exhibit 4 (Durham County's 2001 Business Personal Property Appraisal of IBM Credit's business personal property (by district)), and Durham County's Exhibit 3 (Durham County's Valuation Methods of Procedures – Excerpts from the 2001 Cost Index and Depreciation Schedules).

⁹ Testimony of Ken Joyner, then Durham County Tax Assessor, admitted as an expert in the appraisal of property.

¹⁰ Attachment A to IBM Credit's notice of appeal to the Commission.

Commission and contends that the value of its computer and computer-related equipment was \$96,443,043 as of January 1, 2001.¹¹

6. While under lease to 364 customer accounts in Durham County the computer and computer-related equipment was being used for the intended purpose for which the equipment was designed and was performing the tasks for which the customers intended the computers and computer-related equipment to do.

7. For tax year 2001, IBM Credit retained the services of NACOMEX U.S.A. Inc.¹² to assist in listing its computer and computer-related equipment in Durham County. As a result of IBM Credit's challenge of the assessed value by Durham County, NACOMEX U.S.A. Inc. developed the NACOMEX Report, which includes NACOMEX tables, to determine the value of the computer and computer-related equipment.

8. Mr. Robert J. Zises,¹³ IBM Credit's expert witness, maintained a database (NACOMEX database) as a resource of providing computer valuation information to various clients who would use the information to establish values for their tangible personal property. The sales information contained in Mr. Zises' database was from transactional observations covering a period in excess of ten years and reflects secondary sales (brokerage sales) of computer and computer-related equipment.¹⁴

9. In his report, Mr. Zises provides a summary of the three approaches to value, income approach, market approach (i.e. sales comparison approach) and cost approach, and in his opinion, his market approach is the best method to estimate the value of IBM Credit's computer and computer-related equipment.¹⁵

10. When developing his method of appraisal, Mr. Zises established subsets that were extracted from the NACOMEX database and used in his report. (NACOMEX Report).¹⁶ Mr. Zises testified that the subsets contained less information than was stored in the transactional sales database (NACOMEX Database). Under his method, Mr. Zises exported only a portion of the transactional sales observations that he deemed necessary to complete his analysis. Mr. Zises did not provide any supporting data to confirm his method and did not provide evidence that he considered additional costs associated with the asset.

11. Based upon the exported information contained in the NACOMEX database subset, and other techniques, Mr. Zises developed certain depreciation tables that he believed reflected the valuation of the computer and computer-related equipment based upon the sales

¹¹ Application for Hearing filed with the Commission on January 25, 2002 including Attachments.

¹² NACOMEX U.S.A. Inc. a computer brokerage company that created the NACOMEX database.

¹³ Mr. Robert Zises is the president and owner of NACOMEX U.S.A. Inc. Mr. Zises also testified that he is an independent contractor that works on projects for NACOMEX U.S.A. Inc.

¹⁴ Testimony of Mr. Robert Zises, expert witness for IBM Credit.

¹⁵ IBM Credit's Exhibit 33 (February 15, 2001 NACOMEX Report).

¹⁶ *Id.*

in his database. As stated in his report, the depreciation factors may be used as age/life multipliers to establish market value when applied to the original cost of each IBM asset within the corresponding category and year.¹⁷ Relying on the NACOMEX Report, IBM Credit arrived at the total valuation of its equipment by multiplying the original purchase price of the computer and computer-related equipment by the percent good listed in the NACOMEX tables for the category and age of the equipment.¹⁸

12. The Durham County Tax Assessor and IBM Credit used the same original purchase price and age for each item of IBM Credit's computer and computer-related equipment, but applied different depreciation tables to arrive at the valuations for IBM Credit's computer and computer-related equipment.

13. Under Zises' report, the transactional observation sales used to develop the depreciation factors were gathered from sales by computer dealers, resellers, brokers and computer traders (secondary market sales).¹⁹ Mr. Zises did not consider any factors relative to computers and computer-related equipment being used in the market. Without additional data, the conclusions contained in Mr. Zises' report regarding his depreciation factors being most applicable to the appraisal of IBM Credit's computer and computer-related equipment are not credible or persuasive.

14. Notwithstanding testimony by Mr. Zises that his appraisal method reflects the rapid rate of technological change in the computer field,²⁰ there is no evidence in the record that addresses any design factors inherent in IBM Credit's computer and computer-related equipment which impair the equipment's desirability or usefulness in the current market.

15. The transactional sales observations contained in Mr. Zises' database that were exported into the NACOMEX database subset to determine the percent good of the computer and computer-related equipment categories are not sales of tangible personal property (computers and computer-related equipment) that were in place performing the functions for which the computer and computer related-equipment were designed. As such, the NACOMEX database and information contained in the NACOMEX Report is not relevant to the circumstance of IBM Credit's business dealings (leasing of computer and computer-related equipment) and such information does not impact the current functionality of the equipment or its use in the market as of January 1, 2001.²¹

¹⁷ *Id.*

¹⁸ NACOMEX Report attached as Exhibit A to IBM Credit's Application for Hearing.

¹⁹ Testimony of Mr. Robert Zises on cross-examination by Ms. Chavis.

²⁰ NACOMEX database is a compilation of transactional sales by computer dealers, wholesalers, brokers and computer traders.

²¹ There are also indications that the NACOMEX Report, as applied to IBM Credit's equipment, granted a full year's depreciation to computer equipment that was on average just six months old. *See* Tr. pp. 644-46. That is, IBM Credit's Exhibit 3 shows that some of its equipment was bought in the early months of a year, some in the middle and some near of the year. Thus, as of the assessment date of January 1, 2001, computer equipment purchased during calendar year 2000 was just an average of six months old, not twelve months old. Yet the Zises Report calls for approximately 40% depreciation as of January 1, 2001 for equipment purchased during calendar

16. The above findings (Nos. 1-15) as to Zises' NACOMEX Report, other than minor editing, were made in the Final Decision entered by the Commission on August 29, 2008. *See* Findings 1-4, 8, 10, and 14-22 of August 29, 2008 Final Decision. Such findings have not been set aside on appeal.

17. The Commission also found in the Final Decision entered March 30, 2006, that Zises' report is "not the appropriate methodology" to assess the subject equipment. *See* Finding 8 of March 30, 2006 Final Decision. This finding was not set aside on appeal either.

18. No new evidence of record has been admitted, and the Commission's findings as to the NACOMEX Report's lack of credibility and persuasiveness remain the law of the case. Moreover, the NACOMEX Report is based on the market sales method alone and does not use the income method.

19. The North Carolina Court of Appeals has held that Durham County did not meet the statutory standards required by G.S. § 105-283 in applying Schedule U5 and there is not sufficient evidence in the current record to answer the issues the Court raises about Schedule U5. *See IBM Credit II* at 689 S.E.2d at 491-93. For these reasons, Schedule U5 and Durham County's application of that Schedule to IBM Credit's equipment will not be relied on or discussed further in this Final Decision.

20. IBM Credit also presented detailed factual testimony on the fair market value of its equipment at the evidentiary hearing held before the Commission during the October 10, 2005 - October 13, 2005 and December 14, 2005 - December 16, 2005 regularly scheduled Session of Hearings. These witnesses were (a) Charles J. Lally, Jr., IBM Credit's sales manager for marketing, and (b) Vincent Palmiotto, IBM Credit's personal property manager. Both had over a dozen year's experience in valuing IBM Credit's equipment through sales and refurbishment. *See* Tr. pp. 39-41, 432-433.

21. IBM Credit's evidence showed the following as the values of IBM Credit's computer equipment at issue in this appeal:

- A. IBM Credit acquires the computer equipment from IBM and other vendors at 100% of the cost negotiated by customers. *See* Tr. pp. 44-45.
- B. Most of IBM Credit's computer equipment is leased for three years. *See* Tr. p. 86.
- C. In order to receive favorable income tax treatment as an operating lease, these leases need to end before the equipment has declined to a residual value of 13%. If

year 2000. This appears to be far too much depreciation for a six-month period. A similar approach was followed in earlier years. Since the evidentiary record is not fully developed on this point, the Commission will not make findings on this issue, nor draw conclusions from it.

the value is lower than 13%, the lease will be considered a capital lease, which receives less favorable income tax treatment. See Tr. pp. 76-78.

- D. IBM Credit's computer equipment typically reaches 13% of its original value in 38 to 39 months (i.e. two to three months after three years). See Tr. p. 77. Likewise, this equipment has a value of just under 20% after three years. See Tr. p. 86.
- E. IBM Credit's equipment has a residual value of 3% after five years. See Tr. p. 77.

22. From this evidence, the value of IBM Credit's equipment at issue can be determined and shown on a chart. *See* Exhibit 1, attached hereto. The computer equipment is leased as income-producing property for three years, and its value declines steadily as each monthly lease payment is made.

23. The resale value of IBM Credit's equipment is 13% after 38-39 months. Therefore, the monthly reduction is calculated by taking the total loss in value during the first 38-39 months (87%) divided by 38.5, which equals 2.26%.

24. Likewise, percent good factors can be calculated for each year of acquisition. IBM Credit's Exhibit 3, a full copy of which was produced to the Commission, shows that during the year 2000, some equipment was purchased early in the calendar year, some in the middle and some toward the end. As of the assessment date January 1, 2001, equipment purchased during 2000 had an average age of six months. Equipment purchased in calendar year 1999 had an average age of 18 months on January 1, 2001, and likewise for prior years.

25. For equipment acquired throughout the year 2000, which was an average six (6) months old on January 1, 2001, the amount of depreciation and obsolescence is approximately 14%. This amount represents the monthly reduction in value of 2.26% times six months.

26. For equipment purchased in 1999, which had an average age of 18 months in January 1, 2001, the loss in value was approximately 41% (i.e. 2.26 times 18 months). The loss in value in years four and five occurs at a slower rate because the equipment has lost most of its value in the first three years.

27. IBM Credit's witness testimony is based on years of managerial experience and provides the basis for the market values of IBM Credit's equipment. Exhibit 2 depicts the 2001 percent good for IBM Credit's equipment based on its witnesses' testimony and exhibits. Trending tables recommended by the North Carolina Department of Revenue and utilized by Counties typically are rounded off to the nearest "5" or "0" for each year's percent good. Exhibit 3 depicts such a typical table.

28. Mr. Lally's experience was with mainframes, peripherals and midrange equipment rather than personal computers, while Mr. Palmiotto testified as to all equipment. IBM Credit contended that its equipment should be appraised on the basis of a three-year life and did not present evidence of a different useful life for personal computers.²²

29. Of the three approaches to valuing IBM Credit's computer equipment, the Commission finds that, based on IBM Credit's factual testimony and exhibits, a combination of the market (i.e. sales comparison) and income approaches should be used in this case. That is, the value of the equipment new (i.e. 100%) is shown by market sales as are the residual values testified to by Charles Lally (i.e. 13% and 3%). Since the equipment is typically leased for three years during which time monthly payments are made, the value of the equipment declines steadily as lease payments are made during the three-year term of the leases. Therefore, the income approach mandates a steady rate of decline in value between the sales dates.

30. Exhibit 1 is based on the market and income methods, and shows the true value of IBM Credit's equipment. Using these methods, applicable depreciation and functional and economic obsolescence due to market conditions are measured accurately.

31. The Court of Appeals raised six issues in its Opinion in *IBM Credit II*. While the Commission's responses to these issues can be inferred from the above Findings, specific answers are set forth on Exhibit 4.

32. IBM Credit's factual testimony and exhibits show that the true value of its computer equipment as of January 1, 2001 was \$144,472,252. Exhibit 5 applies the percent good factors to the 100% acquisition costs of the computer equipment.

33. Since IBM Credit's computer equipment 100% cost was \$301,857,733 and its true value as of January 1, 2011 was \$144,472,252, the total deduction to be taken for depreciation and functional and economic obsolescence due to market conditions was \$157,385,481.

Based on the above (a) Statement of the Case and Facts, (b) discussion of the Burden of Proof, and (c) Findings of Fact, the Commission makes the following Conclusions of Law:

1. The burden of proof and the reasons for not using Schedule U5 to appraise IBM Credit's computer equipment are as set forth above.

2. As set out in the Findings above, and found in the two prior Final Decisions of this Commission, the approach presented by the NACOMEX Report is not credible or persuasive. The prior Findings on this Report were not set aside on appeal, and thus remain the law of the case.

²² Personal computers are also less expensive than midrange equipment and mainframes, and thus appear to represent just a fraction of the total cost of IBM Credit's computer equipment.

3. In view of the whole record as submitted, including the testimony from IBM Credit's management personnel and related documentation, Durham County's appraisal method relying on IBM Credit's testimony and evidence and application of a combination of market approach and income approaches result in the correct and true value for IBM Credit's computer equipment.

4. IBM Credit's evidence shows that its equipment has a useful life of three years and shows sales values at the time of acquisition and sales for residual values after three and five years. As income-producing property, IBM Credit's equipment steadily declines in value as each monthly payment is made on the three-year leases. A combination of the market and income methods correctly appraises IBM Credit's equipment.

5. Exhibits 1, 2 and 3 to this Final Decision show, based on IBM Credit's evidence, the decline in value of its computer equipment and computer related equipment over time and the percent good of such equipment as of January 1, 2001.

6. Based on the greater weight of the evidence, Durham County has met its burden to demonstrate that its methods produce the true value of IBM Credit's computer equipment. The County's appraisal methodology is the proper means and method to produce a true value given the characteristics of IBM Credit's computer equipment.

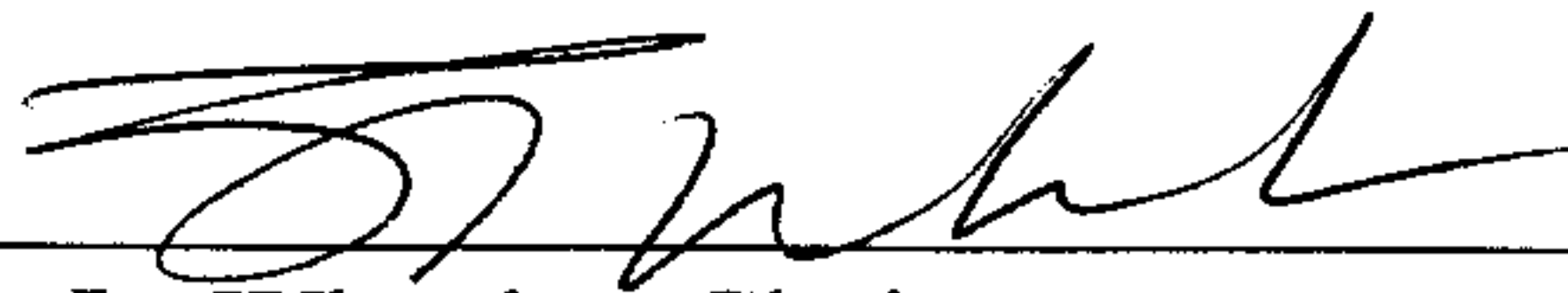
7. The 100% cost of IBM Credit's computer equipment and computer-related equipment was \$301,538,329. The total deduction to be taken for depreciation and functional and economic obsolescence due to market conditions is \$157,385,481 – the difference between the 100% cost and the true value as of January 1, 2001.

8. Exhibit 5 correctly shows the true value of IBM Credit's computer equipment and computer-related equipment as of January 1, 2001 as \$144,472,252.

Based upon the foregoing Findings of Fact and Conclusions of Law, the Commission determines that the true value of IBM Credit's computer equipment as of January 1, 2001 is \$144,472,252.



NORTH CAROLINA PROPERTY TAX COMMISSION

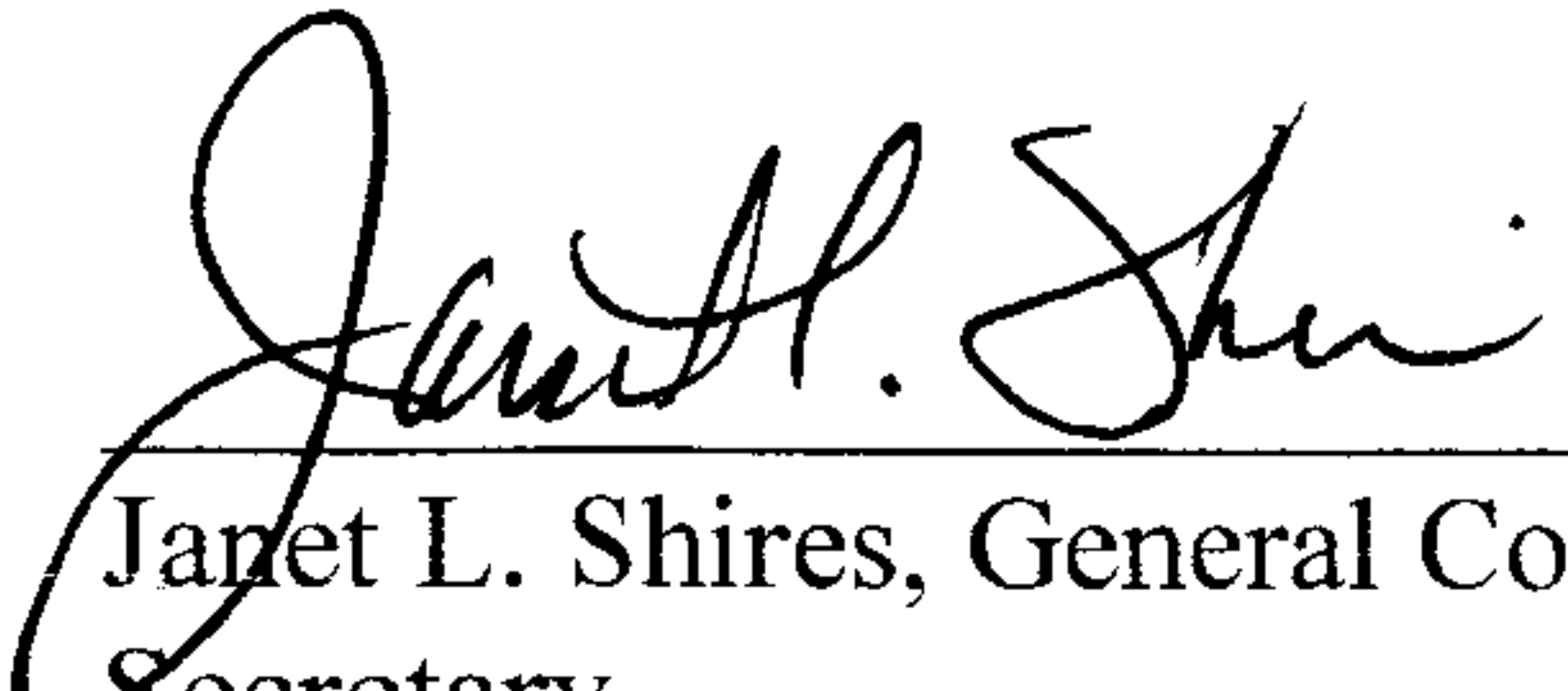


Terry L. Wheeler, Chairman

Vice Chair Plyler and Commissioners Wilmoth, Dixon and Pittman concur.

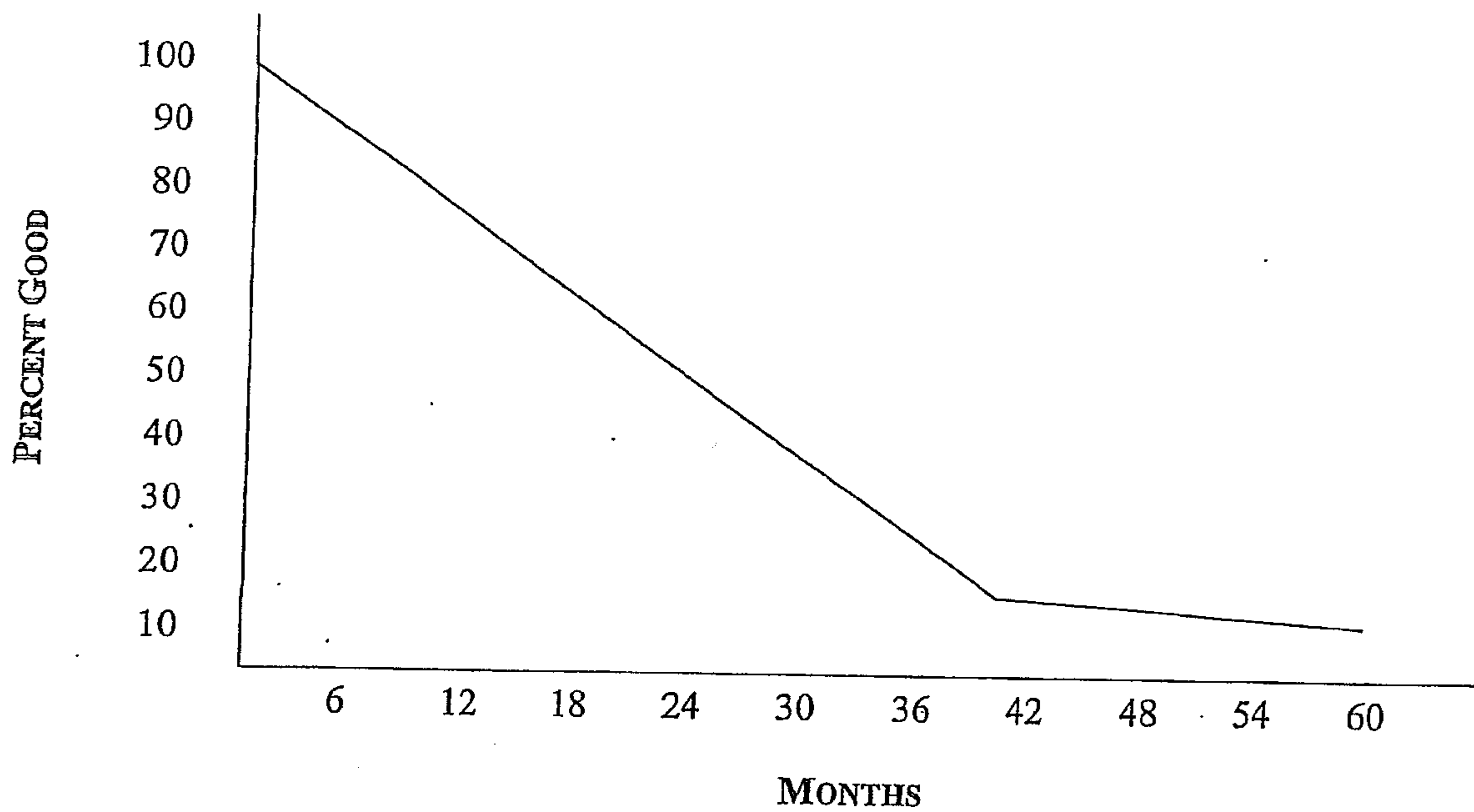
Entered: June 24, 2011

ATTEST:



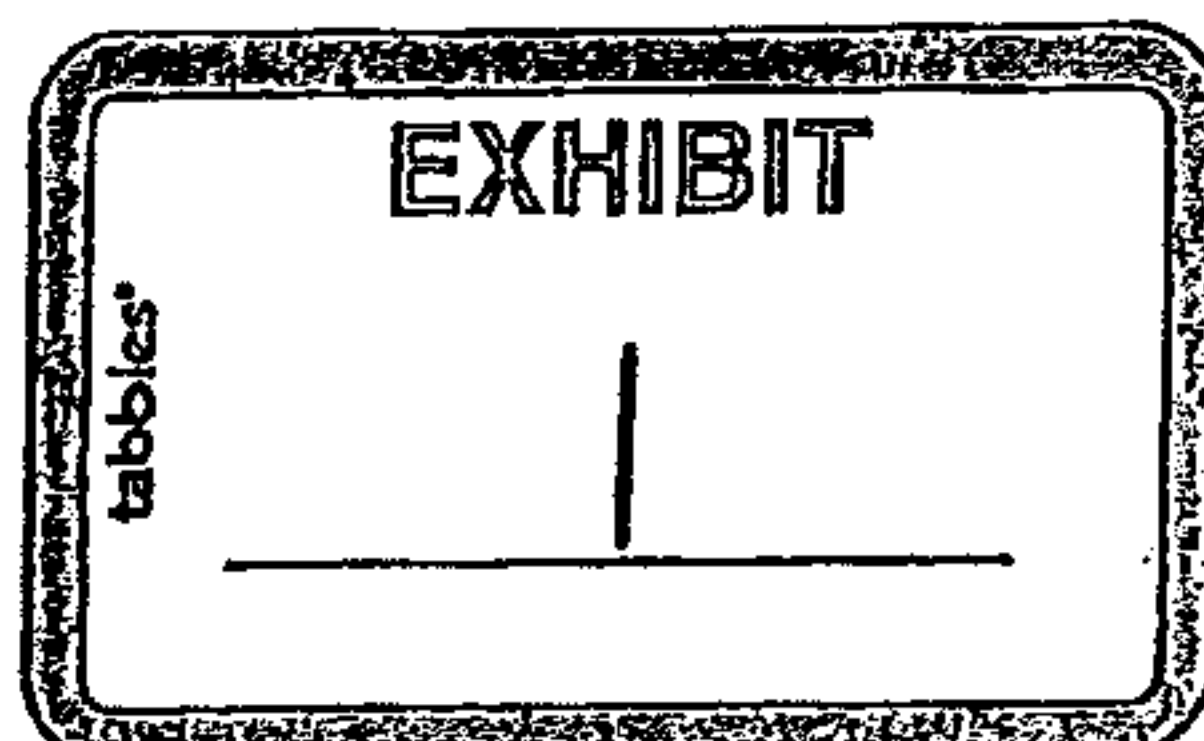
Janet L. Shires, General Counsel and
Secretary

DEPRECIATION AND OBSOLESCENCE
SHOWN BY IBM'S FACTUAL EVIDENCE



* * * * *

1. 100% of value on date of acquisition (Lally, Tr. pp. 44-45).
2. Resale value of 13% after 38 to 39 months (Lally, Tr. p. 77). Decrease in value is 2.26% per month ($87 \div 38.5$)
3. Residual value of 3% at 60 months (i.e. five years). (Lally, Tr. p. 77). Decrease in value of .465% per month from month 38.5 to month 60 ($10 \div 21.5$).
4. Most equipment is leased for three years. (Lally, Tr. p. 86). As income-producing property, the equipment declines in value steadily as each lease payment is made.

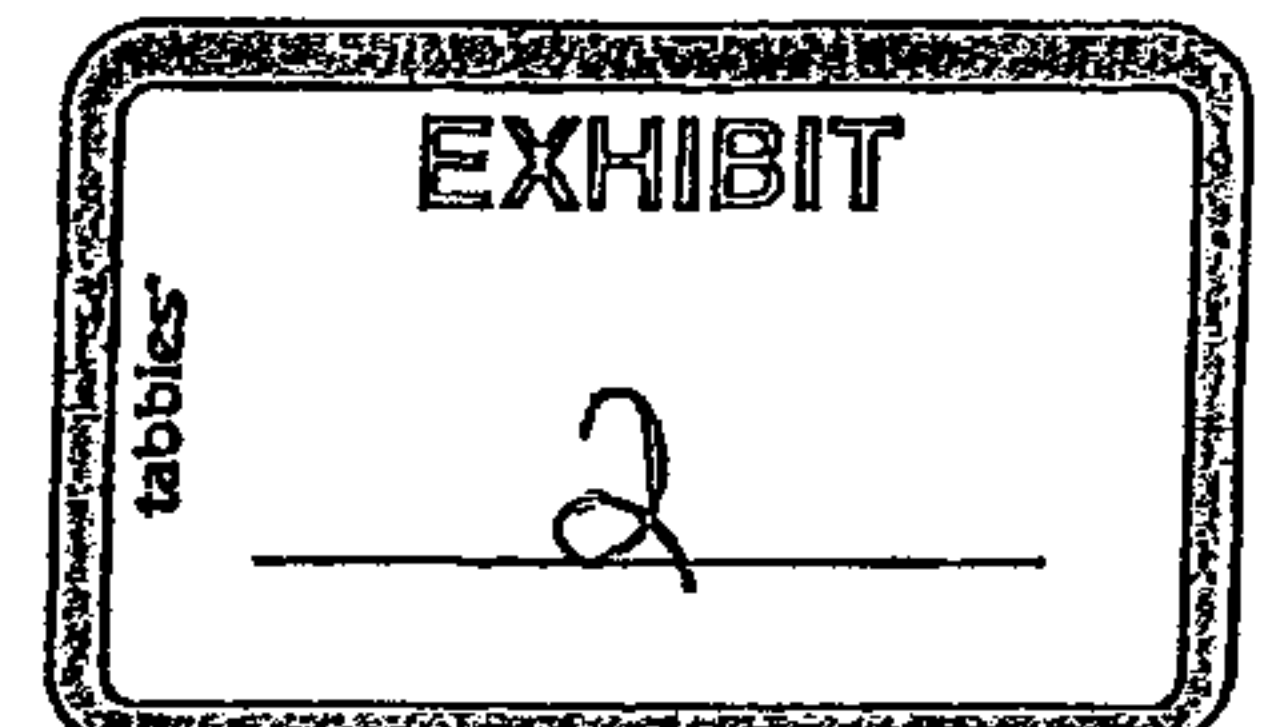


2001 Percent Good
Based on IBM's Evidence

<u>Year Acquired</u> ¹	<u>Percent Good</u> ²
2000	86
1999	59
1998	32
1997	11
1996	6
1995 and before	3

¹ Based on equipment being on average of six months old during the year acquired.

² Percent good factors are based on testimony of IBM fact witnesses.



Updated
2001 Percent Good
Based on IBM's Evidence

<u>Year Acquired</u> ¹	<u>Percent Good</u> ²
2000	85
1999	60
1998	30
1997	10
1996	5
1995 and before	3

¹ Based on equipment being on average of six months old during the year acquired.

² Percent good factors are based on testimony of IBM fact witnesses.

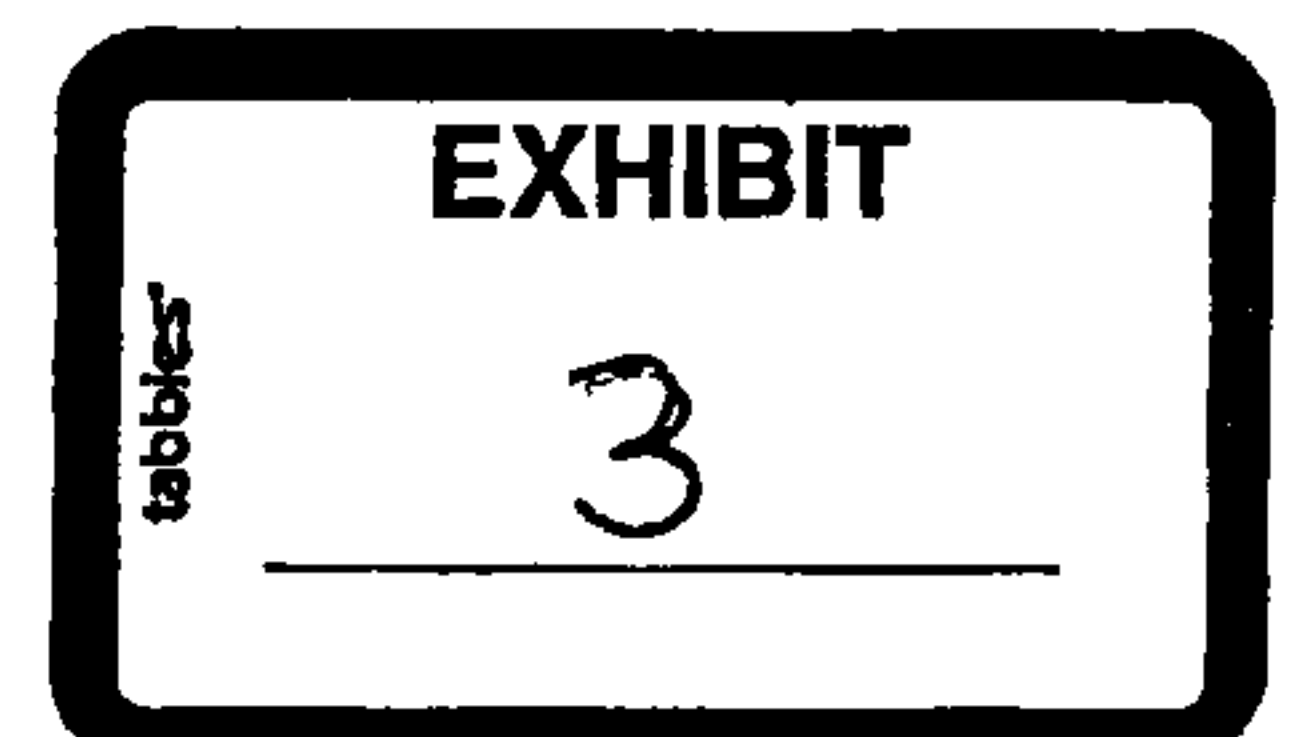


EXHIBIT 4
RESPONSES TO SIX COURT OF APPEALS' ISSUES

Issue 1: Why is the cost approach, as opposed to the sales comparison or income approach, an appropriate means to appraise this property?

Response: The cost approach is not the appropriate means to appraise IBM Credit's property at issue in this appeal given the existing evidentiary record. Based on IBM Credit's testimony of its management personnel, a combination of the market (i.e. sales comparison) and income approaches is the appropriate means to appraise this property.

Issue 2: Why is the income method not employed or used to modify the other approaches?

Response: IBM Credit's factual evidence shows that the income method should be used in conjunction with the market approach.

Issue 3: What is the useful life of the property under appeal?

Response: Three years. While IBM Credit's computer equipment is often sold or refurbished after three years for further use, the equipment loses most of its value during the initial three-year leases, as testified to by IBM Credit's management personnel.

Issue 4: What is the valuation premise behind the 30% deduction in year one of Schedule U5?

Response: The current record does not contain sufficient information to respond to this issue. IBM Credit has opposed the Commission's taking new evidence. This is one reason that IBM Credit's factual evidence of market value, rather than Schedule U5, should be used to appraise the subject equipment.

Issue 5: Why did the facts and circumstances of the valuation not require adjustments for additional functional or economic obsolescence, or other facts, to Schedule U5?

Response: As with Issue 4, the current record does not contain sufficient evidence to respond.

Issue 6: Why does Schedule U5 not use the cost of replacement and reproduction new?

Response: Schedule U5 is no longer being used so any such inconsistency is no longer significant.

Assessed Value of
IBM Credits Computer Equipment

IBM Credit
Account # 3571744
Tax Year

2001

Year of Acq	Cost	Percent Good	Assessed Value
2001	\$ -		
2000	\$ 4,456,688	85	\$ 3,788,185
1999	\$ 3,619,675	60	\$ 2,171,805
1998	\$ 5,483,559	30	\$ 1,645,068
1997	\$ 4,876,900	10	\$ 487,690
1996	\$ 883,313	5	\$ 44,166
1995&Prior	\$ 7,811,566	3	\$ 234,347
Total	\$ 27,131,701		\$ 8,371,260

IBM Credit
Account # 7980599

Tax Year

2001 Percent Good Assessed Value

Yr of Acq	Cost	Percent Good	Assessed Value
2001			
2000	\$ 4,118,998	85	\$ 3,501,148
1999	\$ 6,086,436	60	\$ 3,651,862
1998	\$ 223,670	30	\$ 67,101
1997	\$ 77,868	10	\$ 7,787
1996	\$ 31,582	5	\$ 1,579
1995&Prior	\$ 10,341	3	\$ 310
Total	\$ 10,548,895		\$ 7,229,787

IBM Credit
Account #7980598

Tax Year

2001

Year of Acq	Cost	Percent Good	Assessed Value
2001	\$ -		
2000	\$ 90,596,813	85	\$ 77,007,291
1999	\$ 52,392,162	60	\$ 31,435,297
1998	\$ 48,668,481	30	\$ 14,600,544
1997	\$ 46,728,876	10	\$ 4,672,888
1996	\$ 19,552,137	5	\$ 977,607
1995&Prior	\$ 5,919,264	3	\$ 177,578
Total	\$ 263,857,733		\$ 128,871,205

Total of Accounts

Cost	Assessed Value
\$ 301,538,329	\$ 144,472,252

