

STATE OF NORTH CAROLINA
COUNTY OF WAKE

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

IN THE MATTER OF THE APPEAL OF:

SHELBY MALL, LLC,
Appellant

16 PTC 0462

From the decision of the Cleveland
County Board of Equalization and Review
concerning the valuation of certain real
property for tax year 2016

FINAL DECISION

This matter came on for hearing 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 on Tuesday, June 12, 2018, pursuant to the Appellant’s appeal from the decision of the Cleveland County Board of Equalization and Review (“Board”).

Chairman Robert C. Hunter presided over the hearing, with Vice Chairman Terry L. Wheeler and Commission Members William W. Peaslee and Alexander A. Guess participating.

Attorney Charles C. Meeker appeared on behalf of Cleveland County (“County”). Attorneys Janet L. Shires and George T. Smith, III, appeared on behalf of the Appellant.

STATEMENT OF THE CASE

The properties under appeal are three contiguous parcels, identified by the County by Parcel numbers 70767, 70777, and 70779. Together with the improvements on and to these parcels, the properties are known collectively as the Cleveland Mall, and are generally referred to herein as the “subject property” or simply the “property.”

For each parcel, the Appellant disputed the January 1, 2016 assessed value as determined by the County, and appealed said values to the Cleveland County Board of Equalization and Review (“Board”). On August 30, 2016, the Board determined the combined value of the three parcels to be \$12,000,000, and mailed notice of its decisions to the Appellant on September 27, 2016. The Appellant appealed the decisions of the Board by filing for each property a Notice of

Appeal and Application for Hearing with the Commission on August 3, 2017. Through the respective Notice and Application for each property, the Appellant stated its opinion that the true combined value of the properties was actually \$3,000,000.

ANALYSIS AND ISSUES

A county's ad valorem tax assessment is presumed to be correct.¹ A taxpayer may rebut this presumption by producing "competent, material, and substantial" evidence that tends to show that: "(1) [e]ither the county tax supervisor used an *arbitrary method* of valuation; or (2) the county tax supervisor used an *illegal method* of valuation; AND (3) the assessment *substantially* exceeded the true value in money of the property".² N.C. Gen. Stat. §105-283 requires all taxable property to be valued for tax purposes at its "true value," as that term is defined in the same section.

If the taxpayer produces the evidence required to rebut the presumption, then the burden shifts to the taxing authority to demonstrate that its methods produce true values.³

Under this analysis, the Commission must consider the following issues:

1. Whether the Appellant carried its burden of producing competent, material and substantial evidence tending to show that:
 - (a) The County employed an arbitrary or illegal method of valuation in determining the assessed value of the Appellant's property; and
 - (b) The assessed value substantially exceeded the true value of the property for the year at issue.
2. If the Appellant produced the evidence required to rebut the presumption, then whether the County demonstrated that its appraisal methods produced a true value for the property, considering the evidence of both sides; its weight and sufficiency and the credibility of witnesses; the inferences drawn therefrom; and the appraisal of conflicting and circumstantial evidence.⁴

¹ In re Amp, Inc., 287 N.C. 547, 563, 215 S.E.2d 752, 762 (1975).

² Id. (capitalization and emphasis in original).

³ In re Appeal of S. Ry. Co., 313 N.C. 177, 323 S.E.2d 235 (1985). In re IBM Credit Corporation, (IBM Credit II), 201 N.C. App. 343, 689 S.E.2d 487 (2009), disc. review denied and appeal dismissed, 363 N.C. 854, 694 S.E.2d 204 (2010).

⁴ In re Parkdale Mills, 225 N.C. App. 713, 741 S.E.2d 416 (2013).

**FROM THE EVIDENCE PRESENTED AND ALL DOCUMENTS OF RECORD,
THE COMMISSION MAKES THE FOLLOWING FINDINGS OF FACT:**

1. At the hearing, the Appellant tendered Patrick Muller, a Vice President with the company that managed the subject property for the Appellant, as an expert in the acquisition, valuation, and, management of enclosed malls. The County objected, citing Mr. Muller's lack of certification, licensing, or formal education in these areas. The Commission admitted Mr. Muller as an expert in all three areas.
2. Mr. Muller testified as to the general economic climate in which regional malls operate, and discussed that there are essentially four grades of regional malls, named alphabetically as Class A through Class D. He explained that Class A and B properties were top-tier, investment grade properties; that Class D properties were such investment risks that they couldn't obtaining financing; and that Class C properties fell somewhere in between. Logically, then, whereas the first three classes have upper and lower performance metrics that separate them from each other, Class D has no lower limit—there is no distinction in this approach between one Class D mall that is performing reasonably and another that is in utter ruin, whether physically or financially.
3. Mr. Muller offered his opinion that the income approach was the best appraisal method for determining the value of the subject property. He further testified as to his opinion that the property's value was approximately \$5,700,000, based on a stabilized net operating income of \$954,654, capitalized at a rate of 16.72%. Mr. Muller offered no support for his selection of the capitalization rate, but did note that the rate reflected a provision for local property taxes.
4. On cross-examination, the county demonstrated that the actual net operating income of the property for the year ending December 31, 2015 was \$1,263,977.31, when real estate taxes were removed as an expense.⁵
5. On redirect, Mr. Muller explained as to his opinion that a stabilized net income figure was preferred to actual net income, because he believed that the stabilized number was “more of a market figure than property-specific.”

⁵ The County compared Mr. Muller's information, as provided in Appellant's Taxpayer Exhibit 2, with the Appellant's operating statement, as provided in County Exhibit 17.

6. The Appellant tendered Andrew Robinson, MAI as an expert in real estate appraisal, especially with regard to regional malls. Mr. Robinson was so admitted without objection, the parties having previously stipulated to his sufficiency as an expert. Much of Mr. Robinson's testimony referred to the appraisal report that he co-wrote, and which was admitted for the Appellant as Taxpayer's Exhibit 3.
7. Mr. Robinson testified as to his opinion that the highest and best use of the property was its existing use, and that the sales and income approaches to value were most applicable to this type of property. Mr. Robinson testified as to his opinion of the property's value being \$6,210,000, as the reconciliation of the values determined by the sales comparison and income capitalization approaches.⁶
8. In conducting his sales comparison approach, Mr. Robinson chose a variety of regional mall sales across the country. While all of the sales were apparently of Class D malls, there was significant variation in the relationship between the sale price and the respective property's net operating income. Expressing the relationship as a capitalization rate, the rates for the sales chosen ranged from 12.3% to 27%, more than double that amount.
9. While the income (rather than the sales comparison) approach was the method that both parties' witnesses considered appropriate, Mr. Robinson offered the capitalization rates implied from the comparable sales in supporting his opinion of the appropriate rate at which to capitalize the subject property's net operating income. Mr. Robinson averaged the rates from the comparable sales (17.94%) and compared that rate with two other rate opinions (i.e., 13%+ and 15%+) from unidentified "knowledgeable real estate professionals" to settle on his opinion of a 15% capitalization rate.⁷ When adjusted to account for the local property tax rate, Mr. Robinson's final opinion was that 16.2172% was the appropriate capitalization rate.⁸
10. Finally, Mr. Robinson testified as to his calculation of a stabilized net operating income for the property at \$1,008,835. This figure, capitalized at 16.22%, yields a value estimate of approximately \$6,220,000.

⁶ See Taxpayer's Exhibit 3, at p. 79

⁷ See Taxpayer's Exhibit 3, at p. 76

⁸ See Taxpayer's Exhibit 3, at p. 77

11. The County tendered John T. Bosworth, MAI, SRA, as an expert in real estate appraisal. Mr. Bosworth was so admitted without objection. Much of Mr. Bosworth's testimony referred to the appraisal report that he co-wrote, and which was admitted as County Exhibit 9.
12. Mr. Bosworth testified as to his opinion that the value of the fee simple interest in the subject property was \$12,000,000, and that the value of the leased fee estate was \$9,000,000. He did not elaborate on the distinction between these interests and their respective values, or on the differences between yield capitalization and direct capitalization, although each point was raised.
13. Mr. Bosworth reviewed sale information from several properties that he considered comparable to the subject. He noted that the sales were not helpful in determining a fee simple value, because they were sales of leased fees; however, the sales were useful in developing an overall capitalization rate.
14. Mr. Bosworth testified as to his opinion that the stabilized market-based range of capitalization rates ranged from 12% to 14%; that a stabilized investors survey indicated a capitalization rate range of 9% to 11%; and that a band of investment analysis indicated an overall capitalization rate of 9.77%.⁹ Mr. Bosworth later explained that, although the subject property was not an institutional grade investment, the stabilized investors survey range was above such an investment rate and was appropriate. He also stated that the band of investment analysis (debt to equity) was appropriate because he knew of at least one such property that had been financed, albeit through seller financing. He concluded that 10% was an appropriate capitalization rate.¹⁰
15. Mr. Bosworth originally estimated a net operating income of \$1,152,466 for the subject property. During the hearing, however, he conceded that an error had been made in calculating the potential gross income for the property, in that a \$5.00 per square foot rental rate had been calculated for certain currently vacant space, whereas his intent had been to use a \$2.00 per square foot estimated rent for this space. Recalculating to account for the different rates, Mr. Bosworth revised his opinion, stating that net

⁹ See County's Exhibit 9, at p. 120

¹⁰ See County's Exhibit 9, at p. 120

operating income could be estimated at \$1,067,676, which, when capitalized at a 10% rate, would result in a (rounded) opinion of \$11,000,000 for the final value.

16. We note that, although there was much discussion over the finer details in how each of the three witnesses estimated net operating income for the property, those estimates are all within a narrow range of one another, with the high and low estimates each falling within just a few percent of either the median or average of the three. Overall, we find the revised estimate provided by Mr. Bosworth to be the most detailed of the three, and his figure of \$1,067,676 is the one we have determined appropriate for the subject property.
17. Unlike with the net operating income, the parties differ substantially on their selection of the appropriate capitalization rate by which to convert the estimated net operating income to value. The Appellant's witness suggest a rate in excess of 16%, whereas the County's witness offers a rate of 10%. We note that the Appellant's rate includes a provision for property taxes, but the suggested rate without property taxes is still 15%, a full 50% higher than the County's suggested rate. After much back and forth between each party as to the deficiencies of the other's rate estimate, there was little convincing evidence in favor of either side's suggested rate. We did find, however, that each party's survey of market rates overlapped, and we find that a rate of 13% is supported by evidence from each side. We have not "loaded" the rate with a provision for property taxes, because the income estimate we have selected from Mr. Bosworth's testimony has treated property taxes as an ordinary expense.
18. The value indicated from net operating income of \$1,067,676, capitalized directly at 13%, is \$8,212,893.

BASED UPON THE FOREGOING FINDINGS OF FACT, THE PROPERTY TAX COMMISSION CONCLUDES AS A MATTER OF LAW:

1. The Commission has jurisdiction over the parties and the subject matter of this appeal and has the authority to correct any assessment of real property when it is shown to be based upon an arbitrary or illegal method of valuation and that the valuation substantially exceeds the true value in money.

2. A county's ad valorem tax assessment is presumptively correct.¹¹ The taxpayer rebuts this presumption by presenting "competent, material and substantial" evidence that tends to show that: (1) [e]ither the county tax supervisor used an arbitrary method of valuation; or (2) the county tax supervisor used an illegal method of valuation; and (3) the assessment substantially exceeded the true value in money of the property.¹²
3. The Appellant offered competent, material, and substantial evidence that the Board's values of the subject property substantially exceeded the true value of the subject properties, when the Appellant produced evidence tending to show that the true value of the subject properties was actually about one half of the Board's value.
4. "An illegal appraisal method is one which will not result in true value as that term is used in N.C. Gen. Stat. § 105-283...."¹³ The Appellant offered competent, material, and substantial evidence that the County's appraisal method was illegal when the tax values for each of the subject properties was nearly twice the value suggested by the Appellant's evidence.
5. The Appellant rebutted the presumption of correctness of the assessment of the subject property by the County when the Appellant offered competent, material, and substantial evidence that the County used an illegal appraisal method, and that the County's assessment of the subject property substantially exceeded its true value.
6. Since the Appellant rebutted the presumption of correctness, the burden then shifted to the County to demonstrate that its methods produced true values.
7. "It is generally accepted that the income approach is the most reliable method in reaching the market value of investment property." *In re Appeal of Blue Ridge Mall, LLC*, 214 N.C. App. 263, 269-70, 713 S.E.2d 779, 784 (2011)
8. The County was not able to demonstrate that its methods in appraising the subject property produced true value when its witnesses did not articulate, either by testimony or by documentation, convincing support for its chosen capitalization rate.

¹¹ *In re Amp, Inc.*, 287 N.C. 547, 215 S.E. 752 (1975).

¹² *Id.*

¹³ *In re Appeal of Southern Railway Co.*, 313 N.C. 177, 328 S.E.2d 235 (1985).

WHEREFORE, the Commission herewith orders that the 2016 tax value of the subject properties be changed to a total of \$8,212,893, such figure to be apportioned to the individual parcels in the same manner as was used by the County to apply the previous \$12,000,000 value; and that the Cleveland County abstracts and tax records be changed to give effect to this decision.



NORTH CAROLINA PROPERTY TAX COMMISSION




Robert C. Hunter, Chairman

Vice Chairman Wheeler and
Commission Members Peaslee and Guess concur.

Date Entered: 7/20/18

ATTEST:



Stephen W. Pelfrey, Commission Secretary