BEFORE THE NEBRASKA TAX EQUALIZATION AND REVIEW COMMISSION

SFI LTD. PARTNERSHIP 8, A Nebraska Limited Partnership,	)	
Appellant,	)	CASE NOs. 04C-13 04C-14
vs.	)	
SARPY COUNTY BOARD OF EQUALIZATION,	)	DECISION AND FINAL ORDER AFFIRMING DECISIONS OF COUNTY BOARD OF EQUALIZATION
Appellee.	)	

SUMMARY

SFI Ltd. Partnership 8, a Nebraska Limited Partnership ("the Partnership") owns the Alpine Village Apartment complex in the City of LaVista, Sarpy County, Nebraska. The Partnership protested the Sarpy County Assessor's proposed 2004 values for the Partnership's property to the Sarpy County Board of Equalization ("the Board"). The Board denied the Partnership's protests, and the Partnership appealed to the Commission.

I. ISSUES

The issues before the Commission are (1) whether the Board's decisions to deny the Partnership's valuation protests were incorrect and either unreasonable or arbitrary; and (2) if so, whether the Board's determinations of value were unreasonable.

II.
STATEMENT OF THE CASE

The Partnership owns a parcel of land legally described as Lots 57A and 159D, Park View Heights Addition, City of LaVista, Sarpy County, Nebraska. (E1:1; E4:1). The County Board's determination of actual or fair market value of that parcel is appealed in Case No. 04C-13. The Partnership also owns a tract of land legally described as Lots 159A1, 159A3, 159A4, 159A5, 158 & 57C, and VAC Wilbur Street, Park View Heights Addition, City of LaVista, Sarpy County, Nebraska. (E2:1; E5:1). The County Board's determination of actual or fair market value of that parcel is appealed in Case No. 04C-14. The two tracts of land together total 10.94 acres and are improved with 211 apartments all with interior access; a clubhouse; a pool (which has been closed for two years); tennis courts; laundry facilities; 127 parking garages; and total parking (including the garage spaces) of 450 stalls, for an average of 2.1 parking spaces per unit. (E23:16). The two parcels and improvements constitute the ("subject property").

The Complex was built in two phases. The first phase, completed in 1969, included seven three story "garden" apartment buildings containing 151 apartments. (E23:16). The second phase was built in 1993 and included the remaining 60 units in two apartment buildings. (E23:16).

The Assessor determined that the actual or fair market value of the parcel described in Case Number 04C-13 was $1,950,000 as of the January 1, 2004, ("assessment date"). (E1:1). The Assessor determined that the actual or fair market value of the parcel described in Case Number 04C-14 was $3,960,000 as of the assessment date, for a total of $5,910,000 for both parcels of the subject property. (E2:1). The Partnership timely protested those determinations and alleged that the subject property's actual or fair market value was $4,924,000 as of the assessment date. (E2:2). The Board denied each protest. (E1:1; E2:1).

The Partnership appealed each of the Board's decisions on August 4, 2004. The Commission served a Notice in Lieu of Summons on the Board in each case, which the Board answered. The Commission consolidated the two cases for purposes of hearing and issued an Order for Hearing and later a Third Amended Notice of Hearing. The Commission served a copy of each document on each of the Parties.

The Commission called the case for a hearing on the merits of the appeal in the City of Lincoln, Lancaster County, Nebraska, on December 14, 2005. The Partnership appeared at the hearing through David Slosburg, a Vice President of its General Partner, and through counsel, Jeffrey A. Silver, Esq.. The Board appeared through Tamra L.W. Madsen, Deputy County Attorney. Commissioners Hans, Lore, Reynolds and Wickersham heard the appeal.

Commissioner Reynolds served as the presiding hearing officer. Commissioner Reynolds did not participate in this decision.

The Board, during the course of the hearing, objected to the Commission's receipt of Exhibit 23, the Taxpayer's Appraisal Report and only exhibit, and any testimony by Thomas H. Slack, the Taxpayer's Appraiser ("The Appraiser") alleging that it was possible that the appraisal had been prepared in violation of Nebraska law. The Commission afforded each of the Parties the opportunity to present evidence and argument. The Supreme Court of Nebraska has determined that a statute prohibiting testimony as an appraiser without a license was not intended to affect admissibility of evidence. *See, Hiway 20 Terminal, Inc. v. Tri County Agri-Supply Inc*. 232 Neb. 763, 443 N.W.2d 872 (1989). The Commission accordingly determined that the County's objection went to the weight of Mr. Slack's evidence, not admissibility. Exhibit 23 was received and Mr. Slack was allowed to testify.

III.
APPLICABLE LAW

The Partnership is required to demonstrate by clear and convincing evidence (1) that the Board's decisions were incorrect and (2) that the Board's decisions were unreasonable or arbitrary. Neb. Rev. Stat. §77-5016(7)(Supp. 2005). The "unreasonable or arbitrary" element requires clear and convincing evidence that the Board either (1) failed to faithfully perform

its official duties; or (2) failed to act upon sufficient competent evidence in making its decision. The Partnership, once this initial burden has been satisfied, must then demonstrate by clear and convincing evidence that the Board’s values were unreasonable. *See, Garvey Elevators v. Adams County Bd.*, 261 Neb. 130, 136, 621 N.W.2d 518, 523-524 (2001).

IV.
FINDINGS OF FACT

The Commission finds and determines that:

1. The Partnership stated on the record that the only issue before the Commission is actual or fair market value of the subject property as of January 1, 2004.
2. The Partnership’s evidence of actual or fair market value as of January 1, 2004, is the opinion of an appraiser supported by an appraisal.
3. The Appraiser’s opinion of actual or fair market value for the subject property as of January 1, 2004, without consideration of the Appraiser’s estimated contributory value of personal property is 6.42% less than the Board’s determination of actual or fair market value for the subject property as of that date. (E23:48, E1:1, and E2:1).

V.
ANALYSIS

The income approach is "most suitable for types of properties frequently purchased and held for the purpose of producing income, such as apartments. . .." *Mass Appraisal of Real Property,* International Association of Assessing Officers, 1999, p. 8. The Partnership's Appraiser placed the greatest weight on the Income Approach using a direct capitalization analysis in reaching his opinion of value. (E23:51). The Partnership's Appraiser's Income Approach yields an indicated value of $5,340,000. (E23:51). The County Board also relied on the income approach to determine actual or fair market value as of the assessment date. (E4:3 and (E5:3). The County Board's evidence of value under the Income Approach indicates a total actual or fair market value for the subject property of $5,910,677 as of the assessment date. [$1,952,733 (E4:3) + $3,957,944 (E5:3) = $5,910,677].

The Income Approach can be defined as "a set of procedures through which an appraiser derives a value indication for an income-producing property by converting its anticipated benefits (cash flows and reversion) into property value. This conversion can be accomplished in two ways. One years's income expectancy can be capitalized at a market-derived rate or at a capitalization rate that reflects a specified income pattern, return on investment, and change in the value of the investment.

Alternatively, the annual cash flows for the holding period and the reversion can be discounted at a specified yield rate." *The Dictionary of Real Estate Apprisal*, Fourth Edition, Appraisal Institute, p. 143, (2002). The steps required for use of the income approach with direct capitalization may be summarized as (1) estimate potential gross income; (2) deduct estimated vacancy and collection loss to determine effective gross income; (3) deduct estimated expenses to determine net operating income; (4) divide net operating income by an estimated capitalization rate to yield indicated value. *The Appraisal of Real Estate,* Twelfth Edition, The Appraisal Institute, 2001, pp. 493 - 494. A variety of techniques may be used to determine various components of the approach. *Supra*, chs 20-24, (2001).

The Parties' Income Approaches rely on similar estimates of Potential Gross Income (Partnership $1,389,013; County Board $1,400,040), Vacancy and Collection Loss (Partnership 10%; County Board 10%), and Loaded Capitalization rate (Partnership 12.01%; County Board 12% for the newer portion and 12.50% for the older portion). (E23:48; E4:3; E5:3). Two difference appear in the Parties' use of the income approach, one based on facts and methodology, the other based solely on methodology.

The factual and methodological area of difference is in the determination of expenses. The ratio of total operating expense to effective gross income is the operating expense ratio (OER).

The OER for the subject property as determined by the Appraiser is approximately 51.76%. (Expenses of $712,911 ÷ Effective Gross Income of $1,377,233.) (E23:48). The County Board’s evidence includes a 35% OER for the newer portion of the Complex and 45% for the older portion of the subject property. (E4:3 and 5:3) When combined the product is an OER of 42.14%.([Operating Expenses $126,176 + $404,789 = $530,965] ÷ [Effective Income $360,504 + $899,523 =$1,260,027]). (E4:3 and 5:3). The Taxpayer’s Appraiser’s OER is, therefore, 9.62% higher than the County Board’s OER. It is that difference that largely accounts for variance between the actual or fair market value of the subject property as determined by the County Board and the determination of the Appraiser. The Appraiser based his estimate of operating expenses on an analysis of statements provided by the Partnership and a comparison with information from other apartment complexes. (E23:41-44 and 102-104).

The expense ratios utilized by the County Board were established for tax year 2000 and have not been modified since that year. The Taxpayer’s Appraiser indicated that various cost factors have changed over time including notably, the cost of insurance after the 9/11/01 attacks.

The County Board produced evidence of expense ratios based on sales of apartment complexes. (E12, E13, E14, E15, and E16). Exhibit 12 shows the sale in July of 2002 of an 180 unit

apartment complex built in 1971. At the time of sale the property had an expense ratio before taxes of 39.41%. (E12;1). A 151 units of the subject property were built in 1969. The County Assessor has used an expense ratio of 45% before taxes for that portion of the subject property. (E5:3). The expense ratio before taxes indicated by the sale of a newer and larger complex is lower than the ratio used by the county assessor for the 151 unit portion of the subject property. A newer and larger complex could be expected to have a lower expense ratio because newer complexes have lower repair costs and larger complexes enjoy economies of scale. The higher expense ratio used by the county assessor was to the Partnership's advantage as higher expenses reduce net income and the value based on that income.

Exhibit 15 describes the sale of a 48 unit apartment complex built in 1985. The sale occurred in October of 2000, three years and two months before the assessment date at issue in this proceeding. A 60 unit portion of the subject property was built in 1993. (E23:16) The County used an expense ratio of 35% before taxes for that part of the subject property. (E4:3). The expense ratio before taxes indicated by the sale is 28.59%. (E15:1). The expense ratio before taxes indicated by the sale of an older and smaller complex is lower than the ratio used by the county assessor for the newer portion of the subject property. An older and smaller complex could be expected to have a higher

expense ratio because older complexes have higher repair costs and smaller complexes do not enjoy economies of scale.

The breakdown of components of the County's OER is: 5% management fee; 5% reserves for replacement; 20% miscellaneous; and 5% repairs and maintenance for the newer portion of the subject property; and 15% repairs and maintenance for the older portion of the subject property. (E8:1 and 10:1). Management fees as estimated by the Appraiser are 4.5% (61,976÷1,377,233). (E23:45) Reserves are estimated by the Appraiser to be 4.60% (63,300÷1,377,233). (E23:45). Maintenance is estimated by the Taxpayer's Appraiser to be 13.79% (168,800÷1,377,233). (E23:45). Differences between the Taxpayer's Appraiser's estimates and the County's estimates for those items do not appear to be significant. Payroll costs increased significantly for the subject property in 2003. (E23:102). The Taxpayer's Appraiser did not fully adopt that change in costs but did increase payroll costs above those experienced prior to 2003. (E23:42).

Historical expenses for the subject property can be considered when establishing costs. *The Appraisal of Real Estate*, Twelfth Edition, Appraisal Institute, 2001, p. 493. It is important however to validate those costs with typical expenses for comparable properties. *Id*. Credibility of the Partnership's Appraiser's cost determinations was affected by his failure to obtain market information from apartment complexes not

controlled by the Partnership's general partner. The Commission does not find that the evidence offered by the Partnership of expenses to be deducted in the income approach is clear and convincing or persuasive.

The Appraiser after finding net operating income divided that sum by a capitalization rate of 12.01%. (E23:28). The resulting indication of value was $5,530,992.00 (E23:48). To that point the methodology of the Appraiser and the County Board are identical. The Appraiser, however adopted an additional step. The Appraiser subtracted his estimated contributory value of personal property associated with the subject property ($194,473) from his estimate of capitalized value ($5,530,992) for a resulting final indication of value of $5,336,520. (E23:48).

The Appraiser determined that the contributory value of personal property was 3.5% of the estimated replacement cost new for the project. (E23:28). Replacement cost new less personal property was estimated by the appraiser to be $12,159,263($12,634,013 - 474,750 = $12,159,263). (E23:29) 3.5% of $12,159,263 is $425,574. Depreciated replacement cost of the project less the depreciated value of the personal property was estimated to be $4,584,922. ($4,584,922 - $217,594 = $4,367,328) (E23:29). 3.5% of $4,367,328 is $152,856. The estimated contributory value of personal property is not supported by the

data on page 30 of Exhibit 23. The data on page 30 of Exhibit 23 indicate that personal property would have a higher contribution to value than the Appraiser's estimate. (Costs ($158,250 + $316,500) less Deprecation ($98,906 + $158,250) = $217,594). The contributory value of personal property deducted by the Appraiser is not supported in his appraisal.

The effort of the Appraiser to separate the value of personal property from the real property is logical and has a basis in Nebraska law even if not required by approved appraisal practices, because the real property other than agricultural and horticultural land is subject to tax on its actual value. *Neb. Rev. Stat.* 77-201(1) (Reissue 2003). Personal property is subject to tax on its net book value rather than actual value. *Neb. Rev. Stat.* 77-201(3) (Reissue 2003). The Appraiser's adjustment should not however be adopted without examination. As noted the Appraiser determined the contributory value of the personal property using only one approach, the cost approach. The approach relied on for the final value determination of the real property was the income approach. The Appraiser has shown that it is possible to derive an income approach value for components of the subject property. The Appraiser found for example the net operating income of land by capitalizing a value. (E23:27). A similar technique might have been successful if applied to the personal property value to determine its net

operating income to be subtracted from the effective gross income of the subject property. If for example a 15% rate of return is assigned to the value of the personal property the resulting calculations produce an indicated value for the subject property of $5,249,190 using the other assumptions of the Appraiser as shown in Exhibit 23 page 48. ($194,473 x .15 = $29,170)($1,377,233 - $29,170 = $1,348,063)($1,348,063 - $712,911 = $635,152) ($635,152 ÷ 12.01 = $5,249,190). While the results in this example are similar, any uncertainty concerning the methodology would be eliminated if an estimate of contributory income was made and subtracted.

The second inquiry to be made is whether or not subtracting the value of personal property from the capitalized income results in a double deduction. A deduction for reserves of $300/unit or $63,300 was taken by the Appraiser. (E23:45). Reserves or a replacement allowance may be used for the periodic replacement of items that must be replaced periodically during a buildings life. *The Appraisal of Real Estate*, Twelfth Edition, Appraisal Institute, (2001), p. 487. A replacement allowance may include replacement of stoves, refrigerators etc. *Supra*, at 519, 524, (2001). If the reserve allowance includes the cost of replacing stoves, refrigerator, and dishwashers; two deductions affecting value would be taken for the same item. The first deduction taken would be for contributory value of personal

property and the second for a portion of the purchase of that property. In this case a representative of the Partnership’s general partner testified that the cost of replacing stoves would be included in reserves.

A further concern is consistency in methodology. One income item expressly included in the calculation of effective gross income for the subject property is laundry income. (E23:41). The amount of laundry income is determinable. (E23:102-104). Laundry income is derived from washers and dryers which would be classified as personal property.

Separation of personal property from real property is not always required by the Uniform Standards of Appraisal Practice (USPAP). *Uniform Standards of Appraisal Practice and Advisory Opinions*, The Appraisal Foundation, Standards Rule 1-2(e)(iii), lines 563-564, (2005). Disclosure of personal property included in the value of real property is required. *Id*. Departure from that rule is not allowed. *Id*. lines 536 and 537. USPAP also advises that “An appraiser must analyze the effect on value of any personal property, trade fixtures, or intangible items that are not real property but are included in the appraisals”. *Supra,* Standards Rule 1-4 (g), at lines 667 and 668. Departure from that rule is allowed. *Id*. lines 626-627. A departure must be disclosed. *Id*. lines 402 and 403. The Taxpayer’s Appraiser did not indicate a departure from the rule was being made. The

testimony of the Taxpayer's Appraiser was that he considered the rule binding and that personal property should always be subtracted to avoid overstatement of real property value. The comment to Standards Rule 1-4 (g) gives further guidance. "A separate appraisal developed in compliance with the standard pertinent to the type of property involved, is required when the value of a non-realty item or combination of such items is significant to overall value." *Id*. Comment lines 671-673. Comments are an integral part of USPAP and have the same weight as the component they address. *Supra*. Preamble lines 223 and 224. The Taxpayer's Appraiser did not declare a departure from the comment nor was an appraisal of the personal property involved prepared in accordance with USPAP Standards 7 or 8 concerning the appraisal of personal property. Either the Taxpayer's Appraiser chose to ignore the standards, even though he indicated that his appraisal was prepared in accordance with USPAP, or he did not consider the value of the personal property involved to be significant to overall value. The Commission chooses to believe the latter. Given the difficulty of properly determining adjustments to value for personal property, the possibility of double deductions and inconsistency in the treatment of laundry income the better practice would be to forego an adjustment unless the estimated value of the nonrealty is significant in comparison to the value of the real property

when as in this case they are firmly married in use and income streams. Because a separate appraisal was not prepared for valuation of the personal property as required by USPAP, the Commission concludes the value of personal property was not significant in comparison to the value of the real property.

The County Board did not deduct contributory value of personal property as part of its use of the income approach. If the Taxpayer's Appraiser's deduction for personal property is not considered, the difference between his value determination and the County Board's is $379,685 ($5,910,677 - $5,530,992), a difference of 6.42%.

The Commission may not reverse the decision of the County Board unless, that decision is shown to be arbitrary or unreasonable. Arbitrary has been defined as a decision made in disregard of the facts and circumstances and without some basis which could lead a reasonable person to the same conclusion. *See, Phelps Cty. Bd. of Equal. v. Graf*, 258 Neb 810, 606 N.W.2d 736, (2000). Unreasonable has been defined as a decision for which the evidence presented leaves no room for differences of opinion among reasonable minds. *See, Pittman v. Sarpy Cty. Bd. of Equal.*, 258 Neb 390, 603 N.W.2d 447, (1999). The decision of the County Board was based on mass appraisal techniques used by the Assessor. Those techniques may not take into account the precise characteristics of each parcel even though properly

applied mass appraisal techniques can and do take into account the readily observable and measurable differences between parcels. It is always possible to challenge a value determined through the use of mass appraisal techniques by pointing to the aspects of a parcel that distinguish it from all others. The Courts long ago held that to provide stability in the assessment process that some imprecision would be allowed and that the mass appraisal values would have be granted a presumption of validity. *See, Hastings Bldg. Co. v. Board of Equalization of Adams County*, 190 Neb. 63, 206 N.W.2d 338 (1973). To hold otherwise would have made every challenge to the assessor's value successful on a showing that a given parcel had characteristics different than those assumed by the mass appraisal model. The standard applied by Nebraska courts is reflected in USPAP. "It is implicit in mass appraisal that, even when properly specified and calibrated mass appraisal models are used, some individual value conclusions will not meet standards of reasonableness, consistency, and accuracy". *Uniform Standards of Appraisal Practice and Advisory Opinions*, The Appraisal Foundation, Standards Rule 6-6(b) Comment, lines 1841-1843, (2005). One standard adopted by the Courts to determine whether a value determined by a County Board was unreasonable or arbitrary was whether the evidence established that the value of the County Board was grossly excessive when compared to the value supported by the evidence

before the Court. See, *Hastings* supra. The Commission cannot determine that the difference between the value determined by the County Board and the value supported by the evidence before the Commission, requires a conclusion that the County Board's decision was unreasonable or arbitrary.

VI.
CONCLUSIONS OF LAW

1. The Commission has jurisdiction over the Parties and over the subject matter of this appeal.
2. The Commission is required to affirm the decision of the Board unless evidence is adduced establishing that the Board's action was incorrect and either unreasonable or arbitrary. *Neb. Rev. Stat*. §77-5016(7) (Supp. 2005).
3. The Board is presumed to have faithfully performed its official duties. The Board is also presumed to have acted upon sufficient competent evidence to justify its decisions. These presumptions remain until the Partnership presents competent evidence to the contrary. If the presumption is extinguished the reasonableness of the Board's value becomes one of fact based upon all the evidence presented. The burden of showing such valuation to be unreasonable rests on the Partnership. *See, Garvey Elevators, Inc. v. Adams County Board of Equalization,* 261 Neb. 130, 136, 621 N.W.2d 518, 523 (2001).

4. “Actual value” is defined as the market value of real property in the ordinary course of trade, or the most probable price expressed in terms of money that a property will bring if exposed for sale in the open market, or in an arm’s-length transaction, between a willing buyer and willing seller, both of whom are knowledgeable concerning all the uses to which the real property is adapted and for which the real property is capable of being used. *Neb. Rev. Stat*. §77-112 (Reissue 2003).
5. Actual value may be determined using professionally accepted mass appraisal methods, including, but not limited to, the (1) sales comparison approach using the guidelines in section 77-1371, (2) income approach, and (3) cost approach. *Neb. Rev. Stat*. §77-112 (Reissue 2003).
6. A decision is "arbitrary" when it is made in disregard of the facts and circumstances and without some basis which could lead a reasonable person to the same conclusion. *See, Phelps Cty. Bd. of Equal. v. Graf*, 258 Neb 810, 606 N.W.2d 736, (2000).
7. A decision is “unreasonable” if the evidence presented leaves no room for differences of opinion among reasonable minds. *See, Pittman v. Sarpy Cty. Bd. of Equal.,* 258 Neb 390, 603 N.W.2d 447, (1999).

8. "Clear and convincing evidence means and is that amount of evidence which produces in the trier of fact a firm belief or conviction about the existence of a fact to be proved." *Castellano v. Bitkower,* 216 Neb. 806, 812, 346 N.W.2d 249, 253 (1984).
9. The Partnership has failed to adduce clear and convincing evidence that the County Board's decisions are unreasonable or arbitrary.
10. The Partnership has failed to adduce clear and convincing evidence that the County Board's determinations of value are unreasonable.
11. The Board's decisions must be affirmed.

VII.
ORDER

IT IS THEREFORE ORDERED THAT:

1. The Sarpy County Board of Equalization's determination that the subject property's 2004 taxable value is affirmed.
2. The Partnership's real property legally described as Lots 57A and 159D, Park View Heights Addition, in the City of Lavista, Sarpy County, Nebraska, shall be valued as follows for tax year 2004:

Land	$ 196,043.00
Improvements	$1,753,957.00
Total	$1,950,000.00

3. The Partnership’s real property legally described as Lots 159A1, 159A3, 159A4, 159A5, 158 & 57C, and VAC Wilbur Street, Park View Heights Addition, City of LaVista, Sarpy County, Nebraska shall be valued as follows for tax year 2004:

Land	$ 518,847.00
Improvements	$3,441,153.00
Total	$3,960,000.00

3. Any request for relief by any Party not specifically granted by this Order is denied.
4. This decision, if no appeal is filed, shall be certified to the Sarpy County Treasurer, and the Sarpy County Assessor, pursuant to Neb. Rev. Stat. §77-5016(9)(Supp. 2005).
5. This decision shall only be applicable to tax year 2004.
6. Each Party is to bear its own costs in this matter.

7. This order is final for purposes of appeal February 15, 2006.

Signed and sealed February 15, 2006.

SEAL

____
Wm. R. Wickersham, Chairperson

____
Susan S. Lore, Commissioner

____
Robert L. Hans, Commissioner

ANY PARTY SEEKING REVIEW OF THIS ORDER MAY DO SO BY FILING A PETITION WITH THE APPROPRIATE DOCKET FEES IN THE NEBRASKA COURT OF APPEALS. THE APPEAL MUST BE FILED WITHIN THIRTY DAYS AFTER THE DATE OF THIS ORDER AND MUST SATISFY THE REQUIREMENTS OF STATE LAW IN NEBRASKA REVISED STATUTE §77-5019 (SUPP. 2005). IF A PETITION IS NOT TIMELY FILED, THIS ORDER BECOMES FINAL AND CANNOT BE CHANGED.