

INDIANA BOARD OF TAX REVIEW
Small Claims
Final Determination
Findings and Conclusions

Petition: 45-044-16-1-5-01975-17
Petitioner: Armstrong Family Trust, LLC
Respondent: Lake County Assessor
Parcel: 45-17-16-203-001.000-044
Assessment Year: 2016

The Indiana Board of Tax Review (“Board”) issues this determination, finding and concluding as follows:

PROCEDURAL HISTORY

1. The Armstrong Family Trust, LLC contested the 2016 assessment of its property located at 3461 Highland Court in Crown Point. The Lake County Property Tax Assessment Board of Appeals (“PTABOA”) issued a determination valuing the residential property at \$173,400 (\$29,000 for land and \$144,300 for improvements).
2. The Trust timely filed a Form 131 petition with the Board and elected to proceed under our small claims procedures. On November 5, 2018, Ellen Yuhan, our designated administrative law judge (“ALJ”), held a hearing on the Trust’s petition. Neither she nor the Board inspected the property.
3. Attorney Michael D. Kvachkoff represented the Trust. Hearing Officers Robert Metz and Terrance Dourousseau represented the Assessor. Metz, Dourousseau and real estate broker Alex Nickla were sworn as witnesses.

RECORD

4. The official record for this matter contains the following:
 - a. Petitioner Exhibit 1: Comparative Market Analysis (“CMA”)
 - Petitioner Exhibit 2: 2583 Brookwood Drive rental information
 - Petitioner Exhibit 3: 2583 Brookwood Drive assessment information
 - Petitioner Exhibit 4: 3994 Willowood Court rental information
 - Petitioner Exhibit 5: 3994 Willowood Court assessment information
 - Petitioner Exhibit 6: 1439 Brandywine Road rental information
 - Petitioner Exhibit 7: 1439 Brandywine Road assessment information
 - Petitioner Exhibit 8: Capitalization Rate Calculation
 - Petitioner Exhibit 9: Affidavit of Kevin Koy

Petitioner Exhibit 10: Sale history of 3461 Highland Court
Petitioner Exhibit 11: Valuation history of 3461 Highland Court
Petitioner Exhibit 12: Listing prices of 3461 Highland Court

Respondent Exhibit A: Definition of the income approach
Respondent Exhibit B: Five sales disclosures for the subject property
Respondent Exhibit C: Spreadsheet of comparable sale properties

- b. The record for this matter also includes the following: (1) all pleadings, briefs, motions and documents filed in this appeal; (2) all notices and orders issued by the Board or our ALJ; and (3) an audio recording of the hearing.

BURDEN OF PROOF

5. Generally, a taxpayer seeking review of an assessing official's determination has the burden of proof. Ind. Code § 6-1.1-15-17.2 creates an exception to that general rule and assigns the burden of proof to the assessor in two circumstances—where the assessment under appeal represents an increase of more than 5% over the prior year's assessment, or where it is above the level determined in a taxpayer's successful appeal of the prior year's assessment. I.C. § 6-1.1-15-17.2(b) and (d).
6. Here, the assessed value decreased from 2015 to 2016, and the Trust conceded that it bears the burden of proof.

SUMMARY OF CONTENTIONS

7. The Trust's case:
- a. The Trust presented testimony from Alex Nickla, a real estate broker with Realty Executives in Crown Point. Nickla prepared a CMA for the subject property. He found three rental properties similar to the subject in terms of size, style, and location. The properties rented for \$1,350, \$1,400, and \$1,600 per month, respectively. *Nickla testimony; Pet'r Exs. 1-7.*
- b. Deducting the annual homeowners' association ("HOA") fees and property taxes from each rental property's annual gross rent produced net rents. The net rents were then divided by the assessed values to arrive at a capitalization rate for each rental property. Averaging the cap rates from the three rental properties produced a cap rate of 9.56%.¹ Applying that rate to the subject's net rent of \$11,955.04 resulted in a value of \$125,052 for the subject. *Nickla testimony; Pet'r Ex. 8.*

¹ According to Nickla, the cap rate calculation shown on Pet'r Ex. 8 for 3994 Willowood is incorrect because it used a HOA fee of \$250 when it should have been \$1,285. Using the correct value resulted in a cap rate of 7.87%.

- c. Dividing the subject's net rent by its assessed value of \$173,300 results in a cap rate of 6.89%. The subject's cap rate is significantly lower than the 9.56% average from the three rental properties, indicating that the subject's assessed value is higher than it should be. *Nickla testimony; Pet'r Ex. 8.*
 - d. Beginning in October 2016, Kevin Koy, the Trust's real estate manager attempted to rent the property for \$1,800/month. After two months, he reduced the rent to \$1,600/month. Finally, in April 2017, he located a tenant willing to pay \$1,400/month. In Nickla's opinion, the fair market rent for this property is \$1,400. Nickla agreed the pattern of price reductions indicates the original asking rent was too high and that \$1,400 was a fair value for market rent. *Nickla testimony; Pet'r Ex. 9.*
 - e. The subject property sold four times in a two-year period for prices ranging from \$120,000 to \$130,000. The realtor who sold the property for \$120,000 originally listed it for \$159,900 in December 2015. In June 2016, he reduced the price to \$134,900, and two months later, he reduced it to \$132,900. In August 2016, he finally sold it for \$120,000. If the property was worth \$173,300, there would have been no problem selling it at the original list price of \$159,900. *Nickla testimony; Pet'r Exs. 10 and 12.*
 - f. The photographs that Nickla reviewed showed the interior of the property was in very poor condition and needed a lot of work. But to his knowledge, no work has been done. *Nickla testimony.*
 - g. The Assessor has not shown that his comparable properties are truly comparable because there is no evidence of their condition. If the comps were not foreclosures or REO sales, then they were in perfect, move-in ready condition. Whereas, Nickla's testimony demonstrates that the subject was in shambles in 2016. Thus, arguing that the subject is comparable to properties where people could just move in is ineffective. *Kvachkoff argument.*
 - h. The Trust has met its burden to show that there is something wrong with the property's valuation. The true value of anything is the price that a buyer and seller agree upon, and the subject sold four times in four years for \$130,000 or less. At a minimum, the assessed value should be reduced to \$130,000, which is the price the Trust paid for the property. *Kvachkoff argument.*
8. The Assessor's case:
- a. The Trust's case is based primarily on the income capitalization approach, but its method of calculating cap rates is incorrect. The formula for the income approach is $\text{Value} = \text{Income} / \text{Rate}$. Value refers to market value, which is the amount for which the property sold. Income refers to net operating income. And rate refers to the cap rate. Assessed values play no role in the development of cap rates, but the Trust used assessed values to calculate cap rates. Instead, it should have used market value.

Since none of the Trust's rental comps sold recently, it is impossible to develop a cap rate from them. *Durousseau testimony; Resp't Ex. A.*

- b. Capitalization rates are typically used for multi-unit apartment complexes, not single-family homes. For single-family homes, a gross rent multiplier ("GRM") is more appropriate. A GRM uses a property's gross rent and a multiplier extracted from the market to calculate a value. *Metz testimony.*
- c. The subject property sold four times within a two-year period, but none of the sales were valid. REO sales cannot be considered for purposes of establishing market value unless such sales are the norm in that particular market area. The subject's neighborhood, Lakes of the Four Seasons, is partially located in Lake County and Porter County. On the Lake County side, where the subject property is located, there were 73 sales of single-family homes in 2015. Of those sales, 58 (or 79%) were certified as being valid sales. But the Trust is relying on the four invalid sales of the subject as being representative of its market value-in-use, when only 20% of the sales in the area are REO sales. *Durousseau testimony; Resp't Ex. B.*
- d. The Assessor selected eight comparable sales that were valid, arm's-length transactions. All eight properties were bi-levels built within 13 years of the subject, and they have gross living areas within 11% of the size of the subject's living area. The average price per square foot for the sales was \$67.93, and the median was \$68.12/SF. In contrast, the subject's assessment of \$173,300 represents an assessed value of \$64.76/SF. *Durousseau testimony; Resp't Ex. C.*
- e. The Trust presented no evidence to support the contention that the subject was in terrible condition. *Durousseau testimony.*

ANALYSIS

9. The Trust made a prima facie case for reducing the 2016 assessment. The Board reached this decision for the following reasons:
 - a. The goal of Indiana's real property assessment system is to arrive at an assessment reflecting the property's true tax value. 50 IAC 2.4-1-1(c); 2011 REAL PROPERTY ASSESSMENT MANUAL at 3. "True tax value" does not mean "fair market value" or "the value of the property to the user." I.C. § 6-1.1-31-6(c), (e). It is instead determined under the rules of the Department of Local Government Finance ("DLGF"). I.C. § 6-1.1-31-5(a); I.C. § 6-1.1-31-6(f). The DLGF defines "true tax value" as "market value in use," which it in turn defines as "[t]he market value-in-use of a property for its current use, as reflected by the utility received by the owner or by a similar user, from the property." MANUAL at 2.
 - b. All three standard appraisal approaches—the cost, sales-comparison, and income approaches—are "appropriate for determining true tax value." MANUAL at 2. The

GRM, however, is the “preferred” method of valuing properties with between one and four residential rental units. I.C. § 6-1.1-4-39(b). In an assessment appeal, parties may offer any evidence relevant to a property’s true tax value, including appraisals prepared in accordance with generally recognized appraisal principles. MANUAL at 3; *see also Eckerling v. Wayne Twp. Ass’r*, 841 N.E.2d 674, 678 (Ind. Tax Ct. 2006) (reiterating that a market value-in-use appraisal that complies with the Uniform Standards of Professional Appraisal Practice is the most effective method for rebutting the presumption that an assessment is correct). Regardless of the appraisal method used, a party must relate its evidence to the relevant valuation date. *Long v. Wayne Twp. Ass’r*, 821 N.E.2d 466, 471 (Ind. Tax Ct. 2005). Otherwise, the evidence lacks probative value. *Id.* For 2016, the valuation date was January 1, 2016. Ind. Code § 6-1.1-2-1.5(a).

- c. As explained above, the Trust has the burden of proving that the assessment is incorrect. In support of its contention that the property is over-assessed, the Trust presented an income capitalization approach prepared by Nickla. But Nickla’s analysis relied solely on the subject’s actual rental rate. Although examining the actual rent is an important step, relying on it exclusively is inappropriate when appraising a property’s market value-in-use. *See Indiana MHC, LLC v. Scott Cty. Ass’r*, 987 N.E.2d 1182, 1185-86 (Ind. Tax Ct. 2013) (citing THE APPRAISAL OF REAL ESTATE 493, 501, 509, 511-12 (12th ed. 2001) (“[T]o provide a sound value indication under the income capitalization approach, one must not only examine the historical and current income, expenses and occupancy rates for the subject property, but the income, expenses, and occupancy rates of comparable properties in the market as well.”) (emphasis in original)). Nickla made the same mistake with regard to expenses, and he did not even address vacancy rates. These errors alone deprive Nickla’s income approach of any probative value.
- d. Additionally, we find that Nickla failed to support his capitalization rate. Nickla developed his cap rate using three purportedly comparable rental properties, but he failed to offer any meaningful comparison of their characteristics to those of the subject. *See Long*, 821 N.E.2d at 470 (stating that conclusory statements that a property is “similar” or “comparable” to another property do not constitute probative evidence of the comparability of two properties). We also agree with the Assessor’s criticism that assessed values play no part in the development of cap rates. Because cap rates reflect the annual rate of return required by the market, they are calculated using the ratio of a property’s net operating income to its market value, not its assessed value.
- e. The Trust also argued that the subject property sold multiple times for \$130,000 or less, and ultimately requested that we reduce the assessment to the \$130,000 price it paid for the property on September 23, 2016. The purchase price of a property can be the best evidence of a property’s value. *Hubler Realty Co. v. Hendricks Co. Ass’r*, 938 N.E.2d 311, 315 (Ind. Tax Ct. 2010). Here, the sale closed approximately nine months after the valuation date, and we find it was timely enough to be probative.

- f. In an effort to impeach the sales price, the Assessor submitted sales disclosure forms for four prior sales and the sale to the Trust. While the forms cast significant doubt on the three prior sales that were compulsory transactions resulting from foreclosure proceedings, they fail to undermine the probative value of the sale to the Trust.
- g. The Assessor claimed the sale to the Trust was invalid for trending because the seller, Housemart Biz, Inc., allegedly bought it in a REO sale approximately one month prior to the Trust's purchase. We recognize that some of the reasons a sale might be invalid for trending in the mass appraisal context could also serve as reasons to question whether a sale was an open market, arm's-length transaction. But the Assessor failed to establish that Housemart's purchase was truly a REO sale. Even if the Assessor had, he nevertheless failed to explain how this issue invalidates the subsequent sale from Housemart to the Trust.²
- h. Moreover, the Trust submitted an affidavit from its manager Kevin Koy in which he averred that the \$130,000 purchase price "was negotiated in good faith, no relationship existed between Seller and Armstrong, and no discount was given on the Purchase Price." *Pet'r Ex. 9*. We conclude that the Trust's purchase price was the result of an open market, arm's-length transaction, and that it accurately reflects the property's market value-in-use as of January 1, 2016.
- i. The Trust made a prima facie case that the 2016 assessment should be \$130,000. The burden therefore shifts to the Assessor to rebut the Trust's evidence.
- j. The Assessor presented a sales comparison approach. He selected eight purportedly comparable sales from the Lakes of Four Seasons. But other than providing a basic description of their style, year built, and living area sizes, the Assessor did little to identify their relevant characteristics or compare them to the Trust's property. And he completely failed to explain how any relevant differences affected the values. Thus, the Assessor's sales comparison approach falls well short of providing the level of analysis the Tax Court has explained is necessary when relying on comparative sales data. *See Long*, 821 N.E.2d at 471 (holding that taxpayers' comparative sales data lacked probative value where they failed to compare relevant characteristics or explain how differences affected value). The Assessor therefore failed to rebut the Trust's prima facie case.

² We note that the sales disclosure form documenting the Trust's purchase has the same address listed for both Housemart and the Trust—2929 Jewett Avenue, Highland, IN. That would normally raise concerns that the two entities are related, and make us question whether they truly negotiated at arm's-length. However, the sales disclosure form also lists the address of the Trust's "primary residence" as 362 S. Berkshire, Lake Forest, IL, which corresponds with the address listed for the Trust on its Forms 130 and 131 and the PTABOA's Form 115. Thus, we infer that the use of the Jewett Avenue address for the Trust was a scrivener's error, not an indication that the two entities are related.

FINAL DETERMINATION

In accordance with the above findings of fact and conclusions of law, we find for the Trust and order the 2016 assessment reduced to \$130,000.

ISSUED: April 30, 2019

Chairman, Indiana Board of Tax Review

Commissioner, Indiana Board of Tax Review

Commissioner, Indiana Board of Tax Review

- APPEAL RIGHTS -

You may petition for judicial review of this final determination under the provisions of Indiana Code § 6-1.1-15-5 and the Indiana Tax Court's rules. To initiate a proceeding for judicial review you must take the action required not later than forty-five (45) days after the date of this notice. The Indiana Code is available on the Internet at <<http://www.in.gov/legislative/ic/code>>. The Indiana Tax Court's rules are available at <<http://www.in.gov/judiciary/rules/tax/index.html>>.