

OHIO BOARD OF TAX APPEALS

Board of Education for the)
Berea City School District,)
)
Appellant/Appellee,) (REAL PROPERTY TAX)
)
and)
)
DECISION AND ORDER
)
Manlaw Investment Company, Ltd.,)
)
Appellee/Appellant,) **Reversed and Remanded upon Appeal**
) **Oct. 5, 2005**
vs.) **Ohio Supreme Court**
)
Cuyahoga County Auditor, and)
Cuyahoga County Board of Revision,) **106 Ohio St.3d 269, 2005-Ohio-4979**
)
Appellees.)
)

APPEARANCES:

For the Board of Education - Kadish, Hinkel & Weibel
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Entered November 21, 2003

Ms. Jackson, Ms. Margulies, and Mr. Eberhart concur.

The Board of Tax Appeals is considering this matter pursuant to notices of appeal filed by the Board of Education for the Berea City School District (“BOE”) in case numbers 2003-J-143 and 2003-J-144, and by Manlaw Investment Company, Ltd. in case number 2003-J-150. Appellants have appealed from a decision of the Cuyahoga County Board of Revision (“BOR”) that determined the value of the subject real property for tax year 1997. The property is located in Middleburg Heights and is identified on the auditor’s records as parcel 371-10-004.

The appeals were previously assigned case numbers 1999-J-1920, 1999-J-1921, 1999-J-1942, and 1999-J-1944. This board determined value in the prior appeals by decision entered May 24, 2002. The property owner appealed that decision to the Ohio Supreme Court. On November 26, 2002 the Supreme Court dismissed the appeal pursuant to *Cleveland Elec. Illum. Co. v. Lake Cty. Bd. of Revision*, 96 Ohio St.3d 165, 2002-Ohio-4033. Consistent with the Supreme Court’s order, this board certified the matter to the BOR on December 20, 2002. The parties subsequently filed the within appeals.

On October 10, 2003 this board entered an order requiring the parties to show cause why the appeals should not be decided on the record developed in the prior appeals. The parties failed to respond to the show cause order. Therefore, the appeals have been submitted to the board upon the previous record. The board has reviewed its prior decision and sees no basis for reconsidering it. Accordingly, it is being reissued in substantially the same form.

The value determined by the Cuyahoga County Auditor is as follows:

	TRUE VALUE	TAXABLE VALUE
Land	\$ 651,110	\$ 227,890
Building	\$1,948,890	\$ 682,110
Total	\$2,600,000	\$ 910,000

The value determined by the Cuyahoga County Board of Revision is as follows:

	TRUE VALUE	TAXABLE VALUE
Land	\$ 651,110	\$ 227,890
Building	\$3,548,890	\$1,242,110
Total	\$4,200,000	\$1,470,000

In its notices of appeal the BOE has alleged that the correct value is as follows:

	TRUE VALUE	TAXABLE VALUE
Land	\$ 651,110	\$ 227,890
Building	\$4,848,890	\$1,697,110
Total	\$5,500,000	\$1,925,000

In its notice of appeal the property owner has alleged that the correct value is as follows:

	TRUE VALUE	TAXABLE VALUE
Land	\$ 651,110	\$ 227,890
Building	\$1,948,890	\$ 682,110
Total	\$2,600,000	\$ 910,000

The matter has been submitted to the Board of Tax Appeals upon the notices of appeal, the statutory transcripts certified by the BOR, the evidence adduced at the hearing conducted in the prior appeals, and the briefs submitted by the parties in the prior appeals.

The subject property is located at 17840 Bagley Road, Middleburg Heights, Ohio. It is a 10.719-acre parcel that contains a one-story masonry shopping center building which is divided into a K-Mart store and an in-line store. This building, constructed in 1969, contains 113,100 square feet. Also on the parcel is a 3,454 square foot freestanding Burger King restaurant constructed in 1986.

The property owner purchased the property in March 1996, for \$2,600,000. In *Berea City School Dist. Bd. of Ed. v. Cuyahoga Cty. Bd. of Revision* (Oct. 13, 2000), BTA No. 1996-L-1382, unreported, this board rejected the sale price as not representative of the property's value for tax year 1994. We held:

“In the instant case, the Board finds that although the March 1996 sale appears to be between a willing buyer and seller, the sale was not unencumbered and does not reflect the fee simple value of the subject property.”

Based upon the evidence, this board determined that the value of the property was \$5,000,000 as of January 1, 1994. We further determined that since there had been no change to the property between tax lien date 1994 and tax lien date 1995, the 1994 value was applicable to 1995. Because 1995 was the first year of the triennial period we held that the \$5,000,000 value should carry forward to tax years 1995 and 1996 pursuant to R.C. 5715.19(D).

The BOR considered the complaints filed below and determined that a reduction from tax year 1996 was warranted, finding a value of \$4,200,000. We note that while a determination of value of real property by a board of revision is

entitled to consideration, such determination is not presumptively valid. *Amsdell v. Bd. of Revision* (1994), 69 Ohio St.3d 572. On appeal a party may successfully challenge a determination of a board of revision where the party produces competent and probative evidence which establishes a right to a change in valuation.

In considering the record before us, we acknowledge the affirmative burdens that exist in an appeal to this board from a decision of a board of revision finding value. In *Cleveland Bd. of Edn. v. Cuyahoga Cty. Bd. of Revision* (1994), 68 Ohio St.3d 336, and *Springfield Local Bd. of Edn. v. Summit Cty. Bd. of Revision* (1994), 68 Ohio St.3d 493, the Supreme Court held that in an appeal filed pursuant to R.C. 5717.01, there exists no presumption that the values found by a county board of revision are correct. Nevertheless, an appellant has the burden of presenting evidence in support of the value that it has asserted. Once competent and probative evidence of value has been presented, then the other parties to the appeal have the burden of providing evidence that rebuts that of the appellant. *Springfield Local Bd. of Edn.*, supra; *Mentor Exempted Village Bd. of Edn. v. Lake Cty. Bd. of Revision* (1988), 37 Ohio St.3d 318.

The property owner argued that the price reflected by the March 1996 sale is the best evidence of value. As already discussed, however, this board has determined in *Berea City School Dist. Bd. of Ed.*, supra, that the sale was an encumbered fee and the price did not reflect the fee simple value of the subject property. We must therefore look at the remainder of the record in order to make an independent, de novo, determination of value predicated upon the

preponderance of the evidence submitted. *Coventry Towers, Inc. v. Strongsville* (1985), 18 Ohio St.3d 120.

The property owner submitted the appraisal report and testimony of Robert J. Weiler. Mr. Weiler determined a leased fee value for the K-Mart and a fee simple value for the Burger King.

He used the income approach method of valuation to derive the leased fee value for the K-Mart. K-Mart was occupying 93,333 square feet and subleasing 20,000 square feet of in-line space.¹ K-Mart's lease term was twenty years. As of the tax lien date it had ten years remaining on its lease. In order to estimate whether K-Mart's lease rate was at or near the market rate, he surveyed seven comparable properties to develop an income approach analysis. The seven properties included two WalMarts, a Builder's Square, a Best Products, a Michaels Store, a Dunham's Athleisure, and a Lowe's Home Center. He opined that market conditions have improved slightly; therefore all of the lease rates were adjusted upward for time. The Best Products' and Michaels Stores' leases were adjusted downward to reflect the short-term nature of their lease terms. He adjusted Dunham's downward to reflect its smaller unit size. The Builder's Square, Lowe's Home Center, and WalMart leases were adjusted downward for age, and the Michaels Store and Dunham's were adjusted upward for age. He concluded that overall, on a net basis, \$4.25 per square foot appeared to be a reasonable lease rate for the subject. Since K-Mart's lease rate was \$1.82 per square foot, he concluded that K-Mart had a substantial leasehold interest in the property.

¹ Although the in-line space was being sublet, Mr. Weiler did not conduct a separate analysis for that space.

The K-Mart lease called for overage rent of one percent of gross sales exceeding \$8,235,250. Since he did not know the historical overage rent he relied upon the actual overage rent of \$69,755 paid in 1997. He added this to his gross rental income figure of \$205,805 to produce a total of \$275,560 for potential gross income. He opined that a vacancy and credit loss figure of one percent should be sufficient in reliance upon the fact that K-Mart had a substantial leasehold interest in the property. One percent of the potential gross income produced a figure of \$2,756 for vacancy and credit loss. Deducting \$2,756 from potential gross income produced \$272,804 as effective gross income.

Mr. Weiler's next step was to estimate the expenses. He felt expenses would be stabilized over time. He therefore recomputed expenses and determined \$92,240 as stabilized expenses. He used a fifteen percent replacement allowance influenced by the fact that the roof was leaking as of the effective date of the appraisal. He then calculated net operating income by adding the overage rent of \$69,755 to the \$205,805 potential gross rental income. He deducted operating expenses of \$75,240 and a \$17,000 replacement allowance from the effective gross income, producing \$180,564 as net operating income.

He used an overall capitalization rate of 8.75 percent that was based upon market returns for strong leases such as the subject K-Mart lease. He included a tax additur of 1.88 percent, producing an overall capitalization rate of 10.63 percent. Dividing the \$180,564 net operating income by 10.63 percent produced a rounded figure of \$1,700,000 as the leased fee value of the K-Mart under his income approach analysis.

Mr. Weiler's next step was to conduct a sales approach analysis to derive a value for the Burger King. He gathered sales of three "fast food" establishments, Max & Erma's, Ponderosa Steakhouse, and Long John Silver's. These properties sold in Cuyahoga County between August 1995 and June 1998. The comparables had an unadjusted value range of \$75.93 to \$153.06 per square foot. He opined that market conditions improved slightly and therefore made adjustments from the sale date to the date of the appraisal. He made the adjustments after considering factors such as location, size, land-to-building ratio, age and condition, and quality of construction. He determined that the Burger King was in the middle to upper end of the properties considered, concluding that \$125.00 per square foot was an appropriate value. Multiplying \$125.00 by the Burger King's 3,454 square feet produced a rounded value of \$430,000 for the Burger King. He added the fee simple value of the Burger King to the \$1,700,000 leased fee value he derived for the K-Mart to produce a total value of \$2,130,000 for the property.

The BOE submitted the testimony and appraisal report of Richard G. Racek. Mr. Racek took a different approach than the property owner's appraiser and determined value for the fee simple estate as if unencumbered. He used the market and income approaches to find value.

His market approach analyzed ten sales that occurred between August 1995 and December 1998. His analysis was divided between five properties examined to ascertain value for the K-Mart and five properties examined to ascertain value for the Burger King.

His first sale examined for comparison with the K-Mart was a supermarket that was originally built as a Twin Value store. It was built in 1992 and sold approximately five years later for \$56.28 per square foot. Since he determined it to be in better condition than the subject, he made a negative adjustment to \$40 per square foot.

His second sale was a former Sun TV store. It was built in 1991 and sold in 1998 for \$39 per square foot. He made a negative adjustment because its age and condition were superior to the subject, and made a positive adjustment because the condition of the sale required that it be converted from a retail store to a mini storage building. After adjustments he attributed a unit value of \$38.72 per square foot for this property.

His third sale was a storage building that was vacant when sold on August 24, 1998. Since a large portion of the building was used for storage in relationship to the retail area of the subject, he determined the comparable to be less desirable and made a positive adjustment to account for this factor.

The fourth sale was a retail store that was originally built as a supermarket, then used for a shoe sales facility. It was most recently purchased by an auto dealer that converted the retail building into an auto dealership. It sold for approximately \$38 per square foot of building area on December 21, 1998. The change in use diminished some of the retail potential, which required a positive adjustment.

The fifth sale was a freestanding retail facility that was purchased by K-Mart on September 25, 1995. It was larger and newer than the subject and in

better condition. However, the superior condition of this comparable was offset by the subject's superior location. After analyzing these five sales, he concluded to a unit value of \$40 per square foot of building area including land for the subject K-Mart. He multiplied the subject's 113,100 square feet by the \$40 per square foot unit value, producing a rounded value of \$4,525,000 for the K-Mart.

He next determined a value for the Burger King. He treated the contributory value of the Burger King as an add-on to the total value of the entire site. The first property he examined for comparison with the Burger King was a fast food restaurant that sold several different times. Although its location was superior to the subject's, a positive adjustment for its date of sale, September 1, 1995, offset the negative location adjustment.

The next fast food restaurant sale was a property directly across the street from the subject. It sold on August 15, 1995, was slightly older than the subject, and on slightly more land. He made an adjustment because it needed some interior decorating when it was acquired.

The next sale was a brick building with a basement that sold on January 23, 1996. It was substantially similar to the subject but needed interior decorating. He made a negative adjustment for the basement.

His next comparable was located toward the rear of a shopping center. It sold on July 1, 1996 for \$410,000. It was somewhat older than the subject, in a less desirable area and did not have as much commercial exposure as the subject. It required some interior renovation at the time of its sale. He determined that overall a positive adjustment was required for this comparable.

The final comparable sold on January 31, 1996 for \$410,000. It was a well-located older property that required renovation at the time of sale. He made a positive adjustment to account for these factors.

The restaurant sales developed unit values that ranged from \$26 per square foot of gross building area, excluding land, to a high of \$70.88 per square foot. After reviewing the comparables he concluded that the subject could support a unit value of \$70 per square foot excluding land. He multiplied the subject Burger King's 3,454 square feet by the \$70 to produce a rounded value of \$240,000. Adding the \$240,000 Burger King value to the \$4,525,000 K-Mart value produced a rounded value of \$4,765,000 for the entire property under his market approach analysis.

Mr. Racek's income approach analysis examined ten comparable rental properties that he utilized to estimate fair market rental rate for the subject property. He disregarded the property's current rental rate because it had a commencement date of 1969. He estimated that a rental rate of \$5.00 per square foot of gross building area would be reasonable for the property. He multiplied the subject's 113,100 square feet by the \$5.00 to produce a net potential income for the property of \$565,000 as of January 1, 1997. From this figure he deducted vacancy and credit loss of five percent, which produced an effective gross income of \$537,225. He estimated operating expenses at three percent of effective gross income, including a reserve for future potential leasing commissions, producing a figure of \$16,117. He also estimated a reasonable replacement reserve of \$.30 per

square foot annually or \$33,930. Deducting the expenses from the gross effective income produced a net operating income of \$487,178.

His next step was to determine an appropriate capitalization rate. He extracted his capitalization rate from the market by examining four sales of commercial investment properties. The capitalization rates suggested by these sales ranged from 9.6 percent to 10.6 percent. Based upon his analysis, he concluded an appropriate overall capitalization rate of 10.5 percent would be appropriate.

He then divided the \$487,178 net operating income by the 10.5 percent capitalization rate, producing a rounded value of \$4,640,000 via the income approach for the K-Mart. He then added this value to the \$240,000 contributory value he derived for the Burger King restaurant via the sales comparison approach to produce an overall value of \$4,880,000 for the property.

He then examined four comparable land sales in Middleburg Heights, Broadview Heights, Solon, and Westlake, Ohio to derive a value for the land itself. The prices ranged from \$129,401 per acre to \$300,000 per acre. The sizes of the lots varied from 4.21 acres to 18.734 acres. Based upon these sales he estimated that the subject site could support a unit value of \$200,000 per acre or \$2,145,000.

The subject property was encumbered on tax lien date by two long-term leases. The property owner argued that because the property is encumbered, it is the leased fee value determined in Dr. Weiler's appraisal that should be assigned to the property. We disagree. We reject his opinion of value since it

does not provide true value of an unencumbered fee simple estate. In *Alliance Towers, Ltd. v. Stark Cty. Bd. of Revision* (1988), 37 Ohio St.3d 16, the Supreme Court held “For real property tax purposes, the fee simple estate is to be valued as if it were unencumbered.” (Syllabus, paragraph 1) The court summarized its view of the authorities at page 23:

“These tax and eminent domain cases demonstrate the decision by this court to view the fair market value of real property as uncomplicated by encumbrances. It is the fair market value of the property in its unrestricted form of title which is to be valued. It is to be valued free of the ownership of lesser estates such as leasehold interests, deed restrictions, and restrictive contracts with the government. For real property tax purposes, the fee simple estate is to be valued as if it were unencumbered.”

The Supreme Court relied squarely upon *Alliance Towers* in concluding property be valued as a fee simple estate unencumbered by voluntary restrictions upon common property in a planned unit development. *Muirfield Assn., Inc. v. Franklin Cty. Bd. of Revision* (1995), 73 Ohio St.3d 710. This board has also followed these decisions, determining that Ohio law bases value for ad valorem tax purposes upon fee simple ownership. *Society Bank v. Franklin Cty. Bd. of Revision* (Nov. 24, 2000), BTA No. 1999-M-204, unreported; subsequently settled on appeal, *Society Bank v. Franklin Cty. Bd. of Revision*, (Feb. 20, 2001), S.Ct. No. 2000-2237.

Since the board has determined that it must value the property unencumbered by the leases to K-Mart, it is unnecessary to address the property

owner's alternative argument that a leased fee interest is not subject to taxation under Ohio law.

The BOE submitted probative and competent evidence of value in the testimony and appraisal report of Mr. Racek. The property owner failed to successfully challenge his conclusions and has failed to establish other probative, competent evidence of value. Therefore, based upon a preponderance of the evidence, the Board of Tax Appeals finds that the value of the subject property as of January 1, 1997 is:

	TRUE VALUE	TAXABLE VALUE
Land	\$2,145,000	\$ 750,750
Building	\$2,655,000	\$ 929,250
Total	\$4,800,000	\$1,680,000

The Auditor of Cuyahoga County is ordered to cause his records to reflect the value determined herein for the subject real property and to assess the same in accordance therewith as provided by law.

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