

ORIGINAL

IN THE SUPREME COURT OF OHIO

Board of Education of the Columbus City Schools,

Appellant,

v.

Franklin County Board of Revision,
Franklin County Auditor, and 3600
Sullivant Avenue, LLC.

Appellees.

Case No. 2014-0723

Appeal from the Ohio Board of
Tax Appeal - Case No. 2011-2109

REPLY BRIEF OF APPELLANT
BOARD OF EDUCATION OF THE COLUMBUS CITY SCHOOL DISTRICT

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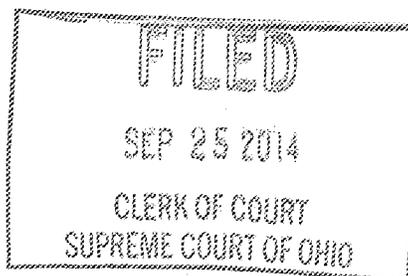


TABLE OF CONTENTS

Table of Authorities iii

Law and Argument.....1

Introduction.....1

1. Moye Erred in Using a Full Tax Additur in a Net Lease Appraisal of the Subject Property.....2

2. Moye Erred in Taking a Dollar-For-Dollar Deduction for Deferred Maintenance.....5

Conclusion.....11

Certificate of Service12

TABLE OF AUTHORITIES

Cases:

Board of Edn. of the Hilliard City Schools v. Franklin Cty. Bd. of Revision (Dec. 15, 2009), BTA Case No. 2007-M-818, 2009 Ohio Tax LEXIS 18843

Board of Edn. of the Hilliard City Schools and Board of Edn. of the Columbus City Schools vs. Franklin Cty. Bd. of Revision, et al. (Aug. 17, 2010), BTA Case 2010-Q-845; 2010-Q-846; 2010-Q-847; 2010-Q-848, 2013 Ohio Tax LEXIS 36473

Board of Edn. of the Columbus City Schools vs. Franklin Cty. Bd. of Revision, (Sept. 5, 2013), BTA Case 2012-Q-1760, 2013 Ohio Tax LEXIS 44133

Dublin City Schools Bd. of Edn. v. Franklin County Bd. of Revision, 139 Ohio St. 3d 193, 199; 2013-Ohio-45436

General Motors Corp. v. Cuyahoga Cty. Bd. of Revision, 74 Ohio St.3d 513, 660 N.E.2d 440 (1996)7

Statutes, Rules and Other Authorities

Adm. Code Rule 5703-25-07(B)6

Adm. Code Rule 5703-25-06(G)6

LAW AND ARGUMENT

Introduction

This appeal demonstrates what happens when the BTA decides an appeal using its new template form decision in which it attempts to resolve all issues in only two operative sentences. In the first sentence, the BTA adopts the property owner's appraisal using three specific criteria that literally have nothing to do with the probative nature of the appraisal evidence; and in the second sentence the BTA holds that any and all objections to the owner's appraisal report have no merit because all such judgments are merely the "subjective judgments" of the appraiser that cannot be subject to challenge by a board of education. By refusing to address any arguments made by the BOE in this appeal, the BTA does nothing more than create work for this Court.

The two issues raised by Appellant in this appeal have nothing to do with the "subjective judgments" of any appraiser, and the BTA clearly erred as a matter of law by refusing to address, to decide, or even to acknowledge the existence of the two fairly simple errors made by the property owner's appraiser, Andrew Moye, in this case. Both of these errors are governed by long-established precedent of the BTA and this Court, and one of errors is essentially a mathematical error. Had the BTA paid some attention to the issues before it and specifically addressed these two issues as it was required to do, and applied its own precedent to these issues, this appeal would most likely never have come before this Court.

The arguments made by the Appellee property owner in its Merit Brief will be addressed by Appellant in the following order: (1) Moye's error in using a tax additur in a "net lease" appraisal of the subject property; and (2) Moye's error in taking a dollar-for-dollar deduction from his appraised value for what he claimed was deferred maintenance.

1. Moye Erred in Using a Full Tax Additur in a Net Lease Appraisal of the Subject Property.

Appellee makes numerous legal arguments concerning the validity of Moye's error in treatment of the tax additur in his "net lease" appraisal of the subject property. But the error made by Moye was not a legal error about which attorneys can argue, but rather it was a simple mathematical error about which no such arguments can be made.

Appellee does not contest the fact that Moye appraised the property on a "net lease" basis. A "net lease" is also referred to as a triple-net lease, in which the tenant or tenants pay all real estate taxes. To value the property on this basis, Moye used a market or economic rental rate of \$1.50 per square foot on a "net basis" (appraisal report, p. 32, Appellant's Supp. 16) and all of Moye's rental comparables were, likewise, "net lease" properties (appraisal, p. 8, Appellant's Supp. 8). Moye failed to include any reimbursement income from the tenant for real estate taxes in his calculation of effective gross income or in net operating income (appraisal, p. 33, 34, Appellant's Supp. 17, 18), yet he took a added a full tax additur of 2.57 percent to his capitalization rate (appraisal, p. 36, Appellant's Supp. 19). This error resulted in an under valuation of the property in the amount of \$526,987, and the correct value of Moye's income approach was \$2,716,987, not \$2,190,000 as set forth in his appraisal at page 36 (Appellant's Supp. 19).

Appellee argues that the BTA has not prohibited an appraiser from using a full tax additur even when the appraiser does not include the tax payments made by the tenants to the property owner or landlord as reimbursed income in the income statement the appraiser uses to value the property (Appellee Brief, p. 9). This statement is incorrect as the BTA has not done this.

In defense of Moye's actions, Appellee cites (Appellee Brief, p. 9) the BTA case of *Board of Edn. of the Hilliard City Schools v. Franklin Cty. Bd. of Revision* (Dec. 15, 2009), BTA Case 2007-

M-818, 2009 Ohio Tax LEXIS 1884 (First Industrial), which contained the following quotation:

The BOE claims that the property owner's appraiser erred when he applied the tax additur in full. However, the property owner's appraiser *included both pass-through income and expenses*. Therefore, the application of a tax additur to the entire value should not cause the value to be different from the non-application of the tax additur. (emphasis added)

The key to this quotation is the fact that the BTA stated that the appraiser "included *** pass-through income" in his income statement. The BTA's reference to "pass-through income and expenses" is a reference to the fact that the property owner passes through the expenses to the tenant and the tenant then passes-through the income to the property owner by making payments to the property. So in *First Industrial*, the appraiser included the tenant's payment of real property taxes as an income item for the property owner, and the appraiser was allowed to take an expense deduction for real estate taxes in the form of the tax additur. Other BTA cases that have expressly held the same thing include *Board of Edn. of the Hilliard City Schools and Board of Edn. of the Columbus City Schools vs. Franklin Cty. Bd. of Revision* (Aug. 17, 2010), BTA Case 2010-Q-845; 2010-Q-846; 2010-Q-847; 2010-Q-848, 2013 Ohio Tax LEXIS 3647; and *Board of Edn. of the Columbus City Schools vs. Franklin Cty. Bd. of Revision, et al.* (Sept. 5, 2013), BTA Case 2012-Q-1760, 2013 Ohio Tax LEXIS 4413.

Appellee also claims that Moye was not given an opportunity to explain his use of the tax additur at the BOR hearing (Appellee Brief, p. 8). However, Moye was specifically asked at the BOR hearing if he had used a "weighted tax additur" (BOR Audio, 9:57), and he stated that he did use a tax additur and he referred to page 36 of his appraisal report where his tax additur is set forth (BOR Audio, 9:57 and 9:58). If counsel for the property owner, who was at the BOR hearing, was concerned that Moye's answer was incorrect or incomplete, then counsel could have asked Moye at

the hearing to explain what he had actually done in his appraisal. Moye's tax additur problem does not involve a burden of proof issue or a legal issue, as is suggested by Appellee in its Merit Brief (p. 9). It is simply a mathematical error that the BTA should have corrected.

Finally, Appellee argues that Moye's error infected only his income approach to value and not his sales comparison approach, which Appellee claims Moye relied on and, thus, the error had no impact on Moye's value conclusion (Appellee Brief, p. 9-10). In fact, Moye used both the income and the market approaches to determine the value of the property. On page 21 of his appraisal report, Moye stated that:

Both the sales comparison approach and the income capitalization approach are used to value the subject property. The conclusions drawn from these approaches are reconciled to arrive at a correlated final value conclusion.

In his appraisal, Moye stated that the sales comparison approach was "given the most weight in the reconciliation" (appraisal report, p. 37). In no sense does this mean that Moye gave the income approach no weight or that he could have rationally arrived at a value of \$2,190,000 using his market approach if he had realized that his income approach was \$2,792,475, and not \$2,190,000.

Moye's original income and market approaches were essentially the same: the sales comparison approach value was \$2,220,000, and the income approach value was \$2,190,000, which is a difference of only \$30,000, or 1.3 percent; and any attempt to distinguish between the two is meaningless. The fact that his corrected income approach value was \$2,716,987 and not \$2,190,000 (a difference of 22.4%) throws Moye's entire appraisal out of kilter and means that the market approach is highly questionable at best. The difference between these two values is so great and so significant that it should have sent Moye, and the BTA, back to the drawing board in order to figure out why the two approaches were so different. This error is so significant that it affects the probative

nature of the appraisal itself.

Lastly, the subject property is rental property. According to Moye (appraisal, p. 19): “As of January 1, 2008 (tax lien day), the subject was 100% occupied by a single tenant.” The property continued to be leased to tenants from January 1, 2008, to the date of the BOR hearing on May 24, 2011, and was leased to tenants on that date. There is no merit to the claim that an income approach to valuing the property was irrelevant and can be disregarded solely in favor of a market approach. In fact, the failure to rely more heavily on the income approach for an income producing property than the sales comparison approach is dubious in its own right.

2. Moye Erred in Taking a Dollar-For-Dollar Deduction for Claims of Deferred Maintenance.

Moye erred in taking a \$700,000 dollar-for-dollar deduction, based on the estimated cost to cure what Moye claimed was ‘deferred maintenance,’ from the bottom line of his both the income and market approaches to value. This deduction was not a valid deduction for real property tax purposes.

A. The validity of Lump Sum Bottom Line Deductions in True Value Appraisals.

Appellee first argues that the BTA was “correct to accept the dollar-for-dollar deduction of \$700,000” (Appellee Brief, p. 6). First, there is no evidence that the BTA “accepted” the deduction because its decision is totally silent on this issue as well as on all other issues involved in this case.

Second, it is clear that taking a lump-sum deduction from the final value estimate in an appraisal is not proper appraisal practice because it means that no one can rely on any of the judgments or any of the market data used in the appraisal to reach the final estimate of value. In the income approach, for instance, Moye estimated that market rent for the subject property would be

\$1.50 per square foot *if, and only if*, a certain number of repairs were made to the property. But as of tax lien day (and as of three and one-half years later), those repairs had not been made; and so what Moye actually appraised was a *hypothetical and non-existent property*. Moye then cited rental rates from five rent comparables to support the assignment of \$1.50 rent to this *hypothetical non-existent property*. This data did not apply to the subject property as it actually existed and did not show what the market rents for the subject property were as it actually existed on tax lien day.

Yet, Moye's duty was to determine market rents for the subject property *as it actually existed on tax lien day*; and not to determine market rents for some *hypothetical non-existent property*. Likewise, the BTA's duty was to determine whether Moye provided any evidence of market rents for the subject property *as it existed on tax lien day*. Adm. Code Rule 5703-25-07(B) proves this point.

This provision states that:

(B) Each lot, tract, or parcel of land, and *all buildings, structures, fixtures, and improvements* to land shall be appraised by the county auditor according to true value in money, *as it or they existed on tax lien date of the year in which the property is appraised*. (emphasis added)

Adm. Code Rule 5703-25-06(G) states the same thing: "If a building, structure, fixture or other improvement to land is under construction on January first of any year, its valuation shall be based upon its value or percentage of completion *as it existed on January first*" (emphasis added). See *Dublin City Schools Bd. of Edn. v. Franklin County Bd. of Revision*, 139 Ohio St.3d 193, 199; 2013-Ohio-4543; 11 N.E.3d 206, ¶ 22.

The same applies to Moye's sales comparison approach. Moye took the same \$700,000 lump-sum deduction from the bottom of his sales comparison value. He took this deduction *after* he had already adjusted his comparable sales for any differences in the "condition" of the subject

property compared to the sales. As to Sale No. 1, Moye said that “the property’s improvements were considered to be in similar condition as the subject’s, and no [condition] adjustment is warranted” (appraisal, p. 29). As to both Sales Nos. 2 and 3, Moye said that these properties “were considered to have superior physical characteristics when compared to the subject” (appraisal, p. 29 and 30), and Moye made downward adjustments to each for “condition” in the amount of ten percent (appraisal, p. 27). After making adjustments for the “condition” of each comparable sale as compared to the subject property, what could Moye have meant when he took a \$700,000 lump-sum deduction for what is nothing more than a difference in “condition”? It means that, once again, Moye’s comparable sales data and the adjustments thereto were directed at a hypothetical non-existent property, and that none of the comparable sales data and the adjustments thereto have any relevance to the value of the subject property as it existed on tax lien day. In effect, Mr. Moye’s \$700,000 bottom line deduction is in fact a double deduction for the condition of the subject property as compared to the sale comparables.

B. The Repair Costs Were Not Necessary for the Property to be used for its Intended Purpose as a Warehouse

Appellee argues that that “the repair costs [Moye’s \$700,000 deduction] in this case were necessary for the property to be used for its intended purpose as a warehouse” (Appellee Brief, p. 7) and that there was “no question that the defects existed and obviously impacted the price a buyer would be willing to pay for the property” (Appellee Brief, p. 9). Furthermore, Appellee uses this argument in an effort to distinguish this Court’s decision in *General Motors Corp. v. Cuyahoga County Bd. of Revision*, 74 Ohio St.3d 513, 515; 660 N.E.2d 440 (1996), where this Court affirmed the BTA’s decision to reject a dollar-for-dollar deduction from value of the property for the cost to

cure alleged defects because “the BTA ruled that GM had not adequately established a diminution in value due to” the alleged defects and because “[t]he BTA could not find any evidence that these defects must be corrected at any given time or that the cost here must be deducted on a dollar-for-dollar basis without any supporting evidence on its effect on market value.” Appellee claims that the present appeal is different because “the repair costs [Moye’s \$700,000 deduction] in this case were necessary for the property to be used for its intended purpose as a warehouse” (Appellee Brief, p. 7).

First, the facts show that it was *not* “necessary” in any sense to replace the claimed items of deferred maintenance in order “for the property to be used for its intended purpose as a warehouse” as Appellee has argued. The property owner’s manager, James Thomas, testified at the BOR hearing that none of the deferred maintenance items that Moye said had to be “replaced” (roof, HVAC, and sprinkler system – see appraisal, p. 18, Appellant’s Supp. 14) had been replaced and that the property still continued to be rented to warehouse tenants and to be used as a warehouse.

Thomas testified that as of the date of the BOR hearing, May 24, 2011, which was three and one-half years after tax lien day (January 1, 2008), the roof had not been replaced, but rather was being repaired on an as needed basis (BOR Audio, 10:02). As to the need to replace the sprinkler system (fire suppression system), Thomas specifically testified that as of May 24, 2011, “the sprinkler system still works” and that he was merely discussing replacement of the system with several contractors (BOR Audio, 10:02). Thomas also testified that the boilers had been repaired, *not replaced*, and that the heat in the building worked, and that only the air conditioning in the office space need to be replaced and that would only cost \$38,000 (BOR Audio, 10:02-10:03).

Thomas further testified that on January 1, 2008 (tax lien day) the property was 100 percent occupied (Moye also stated this in his appraisal, p. 19), and that the property continued to be rented

after tax lien day (BOR Audio 10:05). While Thomas said that the property was “mostly vacant” during 2009, he said that a tenant had leased 160,000 square feet of space in 2010 (BOR Audio, 10:05). Finally, Thomas testified that at the time of the BOR hearing on May 24, 2011, there were tenants in the property, but the property “was not fully occupied” (BOR Audio, 10:05).

Moye prepared his appraisal report on February 26, 2011, and he presumably knew that none of the items that he claimed were deferred maintenance items had been replaced at that time (although the leaks in the roof were being repaired when needed and the heating system had been repaired), but that the property was still being rented to tenants. Consequently, he should have redrafted his appraisal report to account for that fact.

Finally, there is no evidence in the record to support Appellee’s claim that there was “no question that the defects existed and obviously impacted the price a buyer would be willing to pay for the property” (Appellee Brief, p. 9). While Moye claimed that this was true in order to support his dollar-for-dollar deduction of \$700,000, Moye provided no evidence to support this claim.

C. The \$1,200,000 in Repairs Referred to by James Thomas has no Relevance to Moye’s Appraisal or to the True Value of the Property.

Appellee relies heavily on the BOR testimony of James Thomas to prove that Moye’s estimate of \$700,000 was a “conservative estimate” of what was needed to fix the property (Appellee Brief, p. 3, 9-10). Appellee refers to the Thomas’ list of items that needed to be repaired, the cost of which Thomas estimated to be \$1,200,000. However, none of this has any relevance to Moye’s appraisal of the property.

First, Thomas did testify that he prepared a list of suggested repairs that would cost \$1,200,000, but this figure included numerous other items than just the three items of deferred

maintenance referred to by Moye (roof, HVAC, and sprinklers). Thomas' list included making repairs to the docks, dock doors, concrete floors, parking lots (BOR Audio, 10:00), and a renovation of all of the office space and bathrooms, and new plumbing (BOR Audio, 10:14). Some of these items were not in need of repair as of tax lien day. For instance, Thomas said that the parking lots were just "starting" to break up at the time of the BOR hearing (BOR Audio, 10:00). Moye also looked at the concrete floors, office space, the docks, and the parking lots for his appraisal of the property and described all of them in his appraisal report, but did not state that anything was wrong with any of these items (appraisal, p. 15-17, Appellant's Supp. 11-13).

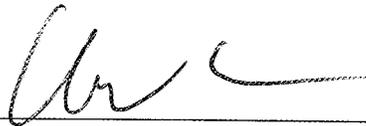
The second significant point of Thomas' testimony is that he specifically testified that if the property owner made all of the repairs that he wanted to make and that would cost \$1,200,000, then "you might be able to get the \$2.25 [rent on a net basis], especially if you find a user that needs a lot of office space" (BOR Audio, 10:14). This has nothing to do with Moye's value because Moye only used \$1.50 per square foot to value the property. The property would be much more valuable under Thomas' scenario because an additional 75 cents in rent would produce an additional \$166,290 in income and produce an extra \$1,700,000 in value, and this value would exceed Moye's value even when \$1,200,000 was deducted off the bottom on the final value conclusion.

In conclusion, valuing the property as a hypothetical non-existent property using market data, such as market rents and comparable sales data, that have no application to the subject property as it existed on tax lien day, and then attempting to correct all of this data by making a lump-sum deduction from the final value conclusion produces only confusion, and insures that no one can know what market data actually applies to the property as it existed on tax lien day.

CONCLUSION

For the reasons set forth herein, this Court is respectfully requested to reverse the decision of the Board of Tax Appeals and to reinstate the Franklin County Auditor's original appraised value of the \$2,750,000 because no evidence exists which proves that the property has any lower or different true value, or in the alternative to remand this appeal back to the BTA with instructions that it address the specific issues raised by Appellant in this appeal and that it render a decision that specifically determines the relevant facts of the matter, and that it set forth those facts in its decision. Finally, Appellant requests this Court to hold that the BTA's use of its new template form decision with the two sentences referred to by Appellant in this Brief is per se unreasonable and unlawful for the reasons set forth herein.

Respectfully Submitted,



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CERTIFICATE OF SERVICE

I hereby certify that a true and complete copy of the foregoing merit brief was served on Karen Bauernschmidt, 1370 West 6th Street, Suite 200, Cleveland, Ohio, 44113, on William J. Stehle, Assistant County Prosecutor, 373 South High Street, 20th Floor, Columbus, Ohio, 43215, and on Mike DeWine, Attorney General, 30 East Broad Street, 25th Floor, Columbus, Ohio, 43215, by regular U.S. mail with postage prepaid, this 25th day of September, 2014.



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