STATE OF MICHIGAN
DEPARTMENT OF ENERGY, LABOR & ECONOMIC GROWTH
MICHIGAN TAX TRIBUNAL
PROPERTY TAX APPEAL

U.S. Can. Hospitalities, LLP,
Petitioner,

v

MTT Docket No. 328350

City of Romulus,
Respondent.

Tribunal Judge Presiding
Victoria L. Enyart

OPINION AND JUDGMENT

Petitioner, U.S. Can. Hospitalities, LLP,, appeals ad valorem property tax assessments levied by Respondent City of Romulus (also "City"), against the real property owned by Petitioner for the 2006 tax year. John R. Hand, attorney, appeared on behalf of Petitioner. Jason C. Long, attorney, appeared on behalf of Respondent. Witnesses appeared on behalf of both parties. They include: Petitioner's valuation expert, Coleen Handlon-Shaull, appraiser and Tony Gabriel, general manager, Ramada Inn. Respondent's assessment expert was Julie Albert, Level IV Assessor.

The hearing was held on June 15, 2009, to resolve the real property assessment dispute.

At issue before the Tribunal is the determination of true cash value of Petitioner's real property for the 2006 tax year. The pertinent information to the contested assessments is as follows:

PARCEL #	AV	TV	PET'S TCV	RESP'S TCV
80-043-99-0005-001	$1,729,000	$1,729,000	$2,870,000	$3,458,000

The Tribunal notes that Respondent did an appraisal that indicates an amended true cash value of $4,061,000.

The interested school districts are Romulus School District and Wayne Intermediate School District. Subject property is addressed as 3119 Flynn, Romulus, Wayne County, Michigan.

Background and Introduction

The subject property is one building with approximately 42,000 to 43,500 square feet located on one parcel identification number, Parcel 80-043-99-0005-001. The property is zoned RC Regional Center District. The 2.18-acre parcel improvements also include parking areas, landscaping and lighting. The subject property was constructed around 1987. Petitioner purchased subject property in 2005, from Fairfield Inn. After the purchase Petitioner obtained a Ramada Inn "flag." The subject property is located at the corner of Merriman Road and Flynn Drive north of I-94. This location is in close proximity to the Detroit Metropolitan International Airport ("DTW"). The subject property has 130 rooms, two meeting rooms and an exercise room.

Petitioner claims some functional factors within the marketplace that would affect the marketability of the subject property. Petitioner states that:

> The subject has on the first two floors it has exterior access to the rooms, and the third floor has interior corridor access to the rooms. So that type of property construction, they aren't really its inferior to interior hallway construction due to safety for the occupants, more control over maybe unwanted patrons at the property, or unwanted activity. TR. p 34.

Respondent did not give any weight to the outdoor access to the rooms on the first and second floors.

Petitioner's Arguments

Petitioner states that the issue is the lawful assessment of the properties. Petitioner contends that the market value of subject property has decreased due to the outdoor access to rooms on the first and second floors, as well as initial year start-up costs.

Petitioner offered P-1, Petitioner's valuation disclosure dated May 15, 2008, TCV as of December 31, 2005.

Petitioner's first witness was Coleen Handlon-Shaull ("Shaull"), certified general appraiser employed by Integra Realty Resources Detroit for 23 years. She assisted Kenneth A. Blondell, MAI, in the preparation of the appraisal used to determine the value of subject property for this appeal. She testified that "My focus has been hotels, hospitality and self-storage. I've done others but those-- hospitality has been my focus." TR. pp 13, 14.

Petitioner's valuation disclosure contains 86 numbered pages and a lengthy unnumbered addendum. The subject property is described as one three-story, limited service hotel containing 130 rooms. The value conclusion is subject to three extraordinary assumptions and limiting conditions: 1. The hotel has been operating as a limited-service midscale-rated Ramada Inn since spring 2005. The appraiser requested, but did not receive, a Property Improvement Plan ("PIP"). The property is in average condition and, as of the date of value, had a $300,000 renovation prior to the affiliation with Ramada Inn. The appraisal was subject to all transfer requirements of the affiliation, including any product plan required by the franchise agreement, a copy of which was not provided; a copy of the Product Improvement Plan ("PIP") was requested

but not received. 2. Management did not report any leased items at the subject, therefore, no lease balances were deducted. It was assumed that accounts receivable and accounts payable were reconciled at closing. 3. The operation of the hotel includes the agreement to provide parking to clients in a stay-and-fly program; thus there are payments for extended parking in airport lots due to the stay-and-fly program at the property with historical operations employing this amenity. The proforma includes continuation of this amenity and program. (In pertinent part, P-1 p 2.)

Shaull determined that the cost approach was not applicable due to the age of subject property, and stated that depreciation estimates would be speculative.

Some of the acronyms used in the appraisal are as follows:

RNS-demand for hotel rooms is measured in "room nights sold."
RNA-hotel room supply is measured in "room nights available."
ADR- average daily room.
RevPar-revenue per available room.

Petitioner states that the primary hospitality competitors are the Howard Johnson, Hampton Inn, Comfort Inn, Quality Inn and the Days Inn. Subject property was in the middle of the competition, until after the competition was rated. Shaull rated the competition giving each amenity "points" with 100 being the maximum. She considered property affiliation (flag), age, condition and perceived cleanliness, exposure, access, convenience to support services, location, security and amenities. Shaull assigned 20 maximum points to the flag, and the remaining amenities 10 points maximum.

Shaull determined that the following points were estimated for each of the hospitality competitors at DTW: Howard Johnson, 78 points; Hampton Inn, 85 points; Comfort Inn, 81 points; Days Inn, 78 points; Subject, 67 points; and Quality Inn, 77 points. She noted that the subject property rated last.

Prior to the sale of subject property, it was operating as a Fairfield Inn. However, Shaull explained that the Fairfield Hotels sold off over a hundred hotels in 2004-2005, because of a management decision to no longer have in their portfolios hotels having exterior access with a Fairfield or Marriott brand. This was categorized as functional obsolescence.

Shaull found sales of limited service hotels in Lower Michigan, because they were not aware of any in the Romulus area near the airport. There were sales after the date of value but they were not utilized. No adjustments were made for any of the comparable sales that were inferior locations in Warren, Kent County, Battle Creek, Hudsonville, Paw Paw, Dundee, Ann Arbor and Chelsea. The nine sales took place from April 2002 to March 2005. The sale price per room ranged from $28,695 (Warren) to $80,952 (Kent County). Shaull states that "The subject's location at the airport is superior to most of the comparable sales." P-1, p 58.

Shaull states that:

> The subject's projected ADR is lower than several of these properties mostly due to its exterior entrances vs. interior corridor access format and/or inferior age or flag vs. an upper-upscale Courtyard flag, or newer, all-suite format with higher ADRs, although the subject is well maintained, and in a superior DTW Airport environs with a stay and park amenity. P-1, p 58.

Shaull determines that the subject's value is below the average based to location and building layout and is $28,000 per room or $3,640,000 via the sales comparison approach.

Petitioner's income capitalization approach utilized the following steps;

- Estimate potential gross income.
  - Multiply the number of rooms by the average daily rate (ADR) multiplied by a projected average annual occupancy.[1]
- Estimate expenses.
- Calculate net operating income from the proforma year.
- Select a capitalization rate from the market to use in the direct capitalization.

Shaull used the subject's financial statements, historical operating statements and Smith Travel Research's *Host* Report.

The following was used to determine the amount of income attributed to room sales: 130 rooms times 365 days equals 47,450 room nights available ("RNA"). 47,450 RNA times 56% occupancy equals 26,572 room nights sold ("RNS"). 26,572 RNS times the average daily rate of $54.00 equals room sales of $1,434,888. Actual sales for 2005 were not available because Petitioner purchased the property after the first quarter, thus only nine months are known. The nine months income is annualized to $1,254,191.

Shaull had information on three properties that were used to compare subject's expenses. She had the operating statements and was able to use them as comparable expenses. Petitioner used national projections[2] for limited service hotels, which show room expenses that range from 2.7% to 24.8%. Shaull utilized 25% room expense recognizing that subject property has higher room expenses for the inclusion of parking fees. Shaull determined that subject's energy costs were higher than typical because of the exterior access for all rooms and the colder Michigan climate. Total expenses used were 65% to 75% based on comparables.

---

[1] The ADR and occupancy are typically based upon historical experience at the subject and data extracted from the marketplace. Additional revenues from other operating departments are then considered. P-1, p 60.

[2] October 2005 *STR Preliminary Industry Performance* stats for Limited Service.

The remaining calculation is the overall rate that considers the quality, quantity and durability of the subject's income. 9.75% was selected as an appropriate capitalization rate for subject's age, location, and condition. This was based on overall rates in the market. Shaull had some sales with capitalization rates that ranged from 9.9% to 13%, a band of investment resulted in a 10% rate, and she selected 9.75% as an overall rate. The equity portion was 30% resulting in a 70% financing ratio by the lender. Twenty years was the amortization period. The effective tax rate (50% of the millage rate) is added to result in a tax neutral capitalization rate of 12.648.

Shaull deducted $14,332 taxes on non-assessable property for an adjusted net operating income of $425,918 for an enterprise value of $3,367,554. Shaull testified that the enterprise value was adjusted for personal property, working capital, start-up costs, inventories, franchise fees, for $494,600 rounded to $500,000. The appraisal termed the adjustments as non-assessables.

Shaull testified to the development of the $500,000 deduction as well as explaining it in the appraisal. She broke the $500,000 into the separate categories and stated that the enterprise value of a going hotel contains more than the tangible real and personal property. A hotel is purchased with some going concern value. Subject property was an operating hotel prior to the purchase. The assessor's personal property was $201,000 and Shaull thought it was reasonable. The working capital was estimated at $75,000.

Some of the costs associated with the going concern are assemblage of the property, equipment and trained employees. Working capital is necessary for the initial 30 days because a new buyer

wouldn't have the advantage of income from selling rooms. Inventory was estimated at $500 per room or $65,000 because franchises require new linens and refurbishing of the rooms. Franchise fees for a Ramada were estimated at $35,000 per year and she accepted that as reasonable.

The $494,600 non-assessables were deducted from the enterprise value for a final value of the real property of $2,870,000.

Respondent's Arguments

Respondent argues that the subject property is not assessed in excess of 50% of market value.

Respondent presented an appraisal by Julie Albert, CMAE IV, assessor for the City of Romulus.

Respondent offered the following exhibits:

R-1 Respondent's valuation disclosure dated February 29, 2008, TCV for December 31, 2005 and December 31, 2006.
R-2 Qualifications of Julie Albert.
R-3 Photograph of Ramada Inn,.
R-4 Photograph of Marriott, 30559 Flynn Dr, Romulus.
R-5 30559 Flynn Drive income information for 2005.
R-6 Photograph of Hilton, 8600 Wickham Rd, Romulus.
R-7 8600 Wickham Road income information for 2005.
R-8 Photographs of 31500 Wick Rd., Romulus.
R-9 Photographs of 9863 Middlebelt Rd., Romulus.
R-10 9863 Middlebelt Road income information for 2005.
R-11 Photographs of Days Inn, 9501 Middlebelt Rd., Romulus.
R-12 Comparable map.
R-13 Reserved.
R-14 Smith Travel Research dated January 1999 to September 2005.
R-15 Hotel Occupancy in Michigan, dated December 2006.
R-16 US Return of Partnership Income Form 1056 for 2005, Petitioner.
R-17 2005 Personal Property Statement.

The following exhibits were offered but not admitted:
R-18 Page 20, Classified Ads, Hotel Journal, November 2007.
R-19 Loopnet- Ramada Inn Romulus Detroit Airport dated October 30, 2008.
R-21 Petitioner's answers to Respondent's First Interrogatories and Requests for Production of Documents.

R-22 Documents provided by Petitioner on July 9, 2007.

Albert testified that she used the cost, sales, and income approaches to value to determine the fair market value of subject property. She did not place great reliability on the cost approach. She amended the appraisal based on incorrect square feet and room count. This resulted in a slight reduction in the true cash value estimate of subject property.

Albert emphasized the importance of the location of subject property and the market influences from the proximity to the international airport. She found six sales including the $4,172,165 sale of subject property. She testified that she read the purchase agreement for subject property. It states on page six that excluded from the sale price was:

> Trade names, trademarks and service marks, Fairfield Inn, Fairfield Inn & Suites, and other such trade names, trademarks or service marks. Tr. pp 160, 161.

Respondent testified that she determined in reviewing the purchase agreement that it was a sale of land, improvements of a furnished but unbranded hotel. Albert deducted from the reported price an amount for the personal property that the prior owner reported. She noted that the current property owners failed to file a personal property statement for 2006.

Albert testified that she looked at each of the sales and considered information provided to her by Marcel Vidovic, a local appraiser who appraises many hotels in the area. She discussed the two pages provided in R-1 that gave some detail about each sale.

Comparable one is subject property and contains 130 rooms, outdoor pool, meeting room, as well as a breakfast room. It sold for $27,020 per room, March, 2005.

Comparable two is a Marriott that is close in proximity to subject property. It contains 245 rooms, indoor pool/whirlpool, fitness center, fifteen meeting rooms, and lounge/restaurant. It sold for $34,770 per room, January, 2004. This property was considered superior to subject property.

Comparable three was a former Hilton that is currently an Embassy Suites. It contains 151 two-room suites, indoor pool, and fitness center and meeting rooms. It sold for $36,670 per room, January, 2006. This property was considered superior to subject property.

Comparable four was a Doubletree and is currently a Metropolitan Inn. It contains 268 rooms, indoor/outdoor pool, fitness center and lounge/restaurant. It sold for $26,720 per room, May, 2006. This property was considered superior to subject property because of the larger amount of rooms.

Comparable five is a Super 8 located approximately two miles southeast of subject property. It contains 63 rooms with a continental breakfast area and no other amenities. It sold for $29,530 per room, August, 2006. This was considered inferior to subject property due to a lack of amenities and an inferior location.

Comparable six is a Days Inn that is also located approximately two miles southeast of subject property. It contains 127 rooms with a fitness center, meeting rooms and a bar/grill. It sold for $25,450 per room, November, 2006. This was considered inferior to subject property due to its inferior location.

Albert focused on the quantitative methods that generalized what the adjustments should be but did not provide the Tribunal with the actual qualitative adjustments for the dollar amount of the adjustments. Albert concluded that, based on the six sales, subject property's TCV is $3,600,000 as of December 31, 2005.

Albert also included a summary sheet from the BS&A software that is used to calculate the cost approach based on the 1998 State Tax Commission Assessor's Cost Manual. The cost sheet for subject property indicates: a land value of $651,920; Hotel-Limited Service cost schedule, class C, average quality, built in 1987, effective age 19 years. The Base cost new is $3,444,795, 68% depreciation for a total depreciated cost of $2,342,461, and an economic condition factor of 1.65 to result in a true cash value of $3,865,060. The land is added to the building for a true cash value of $4,516,980, which results in an SEV of $2,258,490. Respondent's SEV for 2006 is $1,729,000.

Respondent testified that an income approach for a hotel is different from a general commercial property.

> There are attributes that you have to consider. For instance, personal property, and then a business concern or a business value. For personal property I utilized the personal property statements filed by the previous owner, and for business value I considered the management fees and the franchise fees. I used what's called the Rushmore approach. TR. p 185.

When asked if the Rushmore approach is commonly used she responded:

> From what I understand it's used in several states. It's used in Kansas, New Jersey, Maryland, I believe the District of Columbia, bankruptcy courts here in Michigan, bankruptcy court in New York, and I believe the U.S. tax court.

Respondent's income approach started with Smith's Travel Research for 2005. Albert took the number of rooms, multiplied by the daily rate, multiplied by 365 days and then by the level of occupancy. Respondent identified properties used in the Smith Research Travel data as Quality Inn Metro that is currently a Howard Johnson, Comfort Inn, Days Inn, Hampton Inn, and subject property. The Smith Research data was used to determine average occupancy. Albert determined that subject property's 50% occupancy may not be appropriate for the following reasons: subject property sold in 2005, the flag changed from Fairfield Inn to Ramada Inn, several managers in 2005, and the subject property appears to be in the middle of the occupancy range. Albert then used the average daily rate of $55.14 for the Romulus properties. The $55.14 multiplied by the number of rooms times the number of days times the level of occupancy resulted in a potential gross income of $1,700,000.

Albert's next step is to deduct the expenses associated with the property. She used Petitioner's 2005 income tax return. She excluded from the expenses interest, because she was attempting to estimate value on a fee simple interest not a mortgage interest. Depreciation was also excluded because it was a function of income tax reporting and property taxes because that is the issue before the tribunal.

Albert had to forecast the entire 2005 year although Petitioner did not own the property for the entire year. She considered the expenses for advertising, cleaning and maintenance, commission, insurance, utilities, communications, royalty, contract labor and postage. When questioned about the significance in accounting for royalty and management fees in the expense she responded "to account for the business value." TR. p 194. She further explained:

> The franchise fees take into consideration the cost of the flag and the management fees take into consideration the skill necessary to operate the hotel in a competent manner. TR. p 194.[3]

Albert determined that expenses were $1,047,157. The expenses were deducted from the gross income to result in a $687,331 income. The next step was to determine the income attributable to the personal property. She used 4% from Petitioner's pro forma and capitalized the amount of personal property utilizing a 13% capitalization rate, added an effective tax rate for a total deduction of $188,066. The net operating income was $499,324. The capitalization applied was 12% for a revised indication of true cash value of $4,061,000 via the income approach.

Findings of Fact

This section is a "concise, separate, statement of facts" within the meaning of MCL 205.751; and, unless stated otherwise, the matters stated or summarized are "findings of fact" within the meaning of 1969 PA 306, MCL 24.285.

The subject property is a 130-room Ramada Inn with a breakfast area, meeting room and a small fitness area. It is located at 3119 Flynn, Romulus, in a district that consists of hotels and restaurants that serve the Detroit Metropolitan Airport. The subject property was purchased for $4,200,000. R-20, p 6.

Both parties submitted valuation disclosures; however, they were still $1,119,000 apart in true cash value.

[3] Although Respondent testified that she used the "Rushmore" method, this is a description of the method.

Petitioner has the burden of establishing true cash value (MCL 205.737(3); MCL 211.27(1)). Petitioner's sales comparison approach did not contain one property that was located sufficiently close to subject. The importance and influence of the Metro Airport to the hotel district was lightly touched on in Petitioner's appraisal.

> The subject's location at the airport is superior to most of the comparable locations. P-1, p 58.
>
> The subject's projected ADR is lower than several of these properties mostly due to its exterior entrances vs. interior corridor access format and/or inferior age or flag vs. an upper-upscale Courtyard flag or newer, all-suite format with higher ADRs, although subject is well maintained, and in a superior DTW Airport environs with a stay and park amenity. P-1, p 58.
>
> Accordingly, the subject's value is judged to be below the average of the comparables discussed herein, due primarily to the location and the building layout. P-1, p 59.

Petitioner made no adjustments to the sale comparables. Petitioner did on P-1 p 58 discuss the differences in the sales and subject. Petitioner did not provide the Tribunal with a document or testimony that explained the $28,000 per room conclusion. The layout was explained as all of the sales have interior corridor access, which are superior to the subject's older construction exterior balcony access. The Tribunal finds Petitioner's sales comparison approach lacking in detail, analysis and consideration of location.

> Market analysis-a process of examining the demand and supply of a property type and the geographic market area for that property type. Appraisal Institute, *The Appraisal of Real Estate*, (Chicago, 13th ed, 2008), p173.
>
> The location of a hotel often indicates the likely clientele.
>
> Airport hotels and highway orientated hotels cater to transient guests. Appraisal Institute, *The Appraisal of Real Estate*, (Chicago, 13th ed, 2008), p198.

Petitioner, with minimal discussion, concluded to the $28,000 per room value based on sales of property located in Kent County, smaller jurisdictions, and areas without the airport influence.

This, coupled with the fact that no adjustments were made to the individual properties, gives the sales comparison approach minimal weight.

Respondent's sales comparison approach found sales of hotels in the airport area. Respondent discussed also, in one page the comparable properties and if the amenities were superior or inferior to subject property. Respondent reached a conclusion of $27,692 per room. Respondent also did not discuss how the conclusion was reached. Respondent's sales comparison approach is afforded minimal weight.

The Tribunal finds that both parties left out a critical part of the sales comparison approach that is the analyzing and adjusting comparable sales. The sales comparison approach is:

> The process of deriving a value indication for the subject property by comparing similar properties that have recently sold with the property being appraised, identifying appropriate units of comparison, and making adjustments to the sale prices (or unit prices, as appropriate) of the comparable properties based on relevant, market-derived elements of comparison. Appraisal Institute, *The Appraisal of Real Estate*, (Chicago, 13th ed, 2008), p 297.

Petitioner's income approach followed the appropriate steps but added property taxes on the non-assessables to the net income before property taxes. The non-assessables included franchise fees which were already included as part of Petitioner's proforma expenses, therefore, the Tribunal will not include the franchise fees as part of Petitioner's non-assessable value.

Petitioner, after the capitalization of the net operating income, determined a value of $3,250,000.

Petitioner's reconciliation is $3,370,000. The allocation of enterprise value of hotel is Petitioner's final step. Petitioner's belief is that the enterprise value of an on-going concern values more than the tangible real and personal property. Petitioner states:

> In the appraisal problem at hand, the subject is an established operating concern, an Enterprise. An operating hotel is a complex organization of many elements including the assemblage of property, plant and equipment and trained employees. The assemblage and start-up of these resources requires time and expertise. The cost of assembling the organization is defined in the hotel accounting statements as pre-opening and opening expenditures. These are the pre-opening expenditures made prior to the opening of the hotel, such as the transferring in or hiring of some experienced employees, salaries and wages before opening, and pre-opening promotions. P-1, p 78.
>
> A reasonable projection of these costs follows. Working Capital is estimated at approximately $75,000, or approximately one month of expenses excluding taxes and reserves. Inventories for non-taxable tangible personal property such as bedding, paper supplies, maid uniforms, etc., are estimated at $500 per room or $65,000 rounded. Pre-Opening and Start-up Costs are projected at $1,000 per room or $130,000 rounded. FF&E are estimated in line with the 2005 personal property assessment, which is approximately $1,500+ per room or $190,000 (rd.) and includes beds, televisions, dressers, night stands, etc., in guest rooms, meeting and breakfast room furniture etc. The franchise fee for a Ramada Inn was reported at $35,000. P-1 p 79.

Petitioner deducts $500,000 for the allocation of non-assessables from the $3,370,000 for a true cash value of $2,870,000.

The Tribunal finds that the franchise fee has been double-deducted, first in the income approach and then again from the non-assessable category.

Respondent's Rushmore method was not discussed in any great detail but is based on an appraisal method that considers the business practices in the hotel industry and how it differs from other business enterprises and does a step-by-step valuation of a hotel. The author, Steven Rushmore, MAI, CHA, has written textbooks and conducted seminars on hotel market analysis

and valuation for the Appraisal Institute. Rushmore and his Rushmore method of valuing hotels has been accepted in New Jersey, Kansas, New York, Michigan, and the U.S. Tax Court as a recognized method for extracting business value by subtracting from the hotel revenues the amount paid by the owner to a management company pursuant to the management contract. The Court of Appeals of the State of Kansas in *Marriott Corporation v Board of County Commissioners of Johnson County*, No. 78,393, (January, 1999) cited the following seven cases that deferred to the Rushmore method of valuing hotels:

Hull Junction Holding Corp v Princeton Borough, 16 N.J. Tax 68, 84 (1996), a property tax appeal, the court quoted from Rushmore's book when discussing hotel valuation.

Prudential Ins v Tp of Parsippany, 16 N.J. Tax 58, 60 (1995), both parties used Rushmore's method to determine net operating income and eliminate the income recognized to result from personal property and business value.

J.F.K. Acquisitions Group, 166 Bankr, 207, 209 (Bankr. E.D.N.Y. 1994), Rushmore was termed by the court "a well recognized and eminent expert in the field of hotel appraisers."

Grand Traverse Development Co., Ltd. Partnership, 150 Bankr. 176, 180 (Bankr, W.D. Mich 1993), Rushmore was the court-appointed appraiser.

Glenpointe Assocs v Teaneck Tp., 10 N.J. Tax 380, 390 (1989), the court cited Rushmore's hotel valuation guide as an authority. In addition, the court recognized and found reasonable Rushmore's method for extracting business value by subtracting from hotel revenues the amount paid by the owner to a management company pursuant to the management contract. 10 N.J. Tax at 391.

District of Columbia v Wash Sheraton Corp, 499 A2d 109, 113 (D.C. 1985), both parties' experts recognized Rushmore as a leading authority in the field of valuation of hotels.

Estate of Slutsky v C.I.R., T.C. Memo 11983-578, 16 (U.S. Tax court 1983), an expert used the Rushmore model to appraise a hotel.

Petitioner's appraiser identified "non-assessable" items; the Tribunal finds the proper terminology is business value. This is defined as:

> Business value-A going concern is an established and operating business with an indefinite future life. For certain types of properties (e.g., hotels and motels,

> restaurants, bowling alleys, manufacturing enterprises, athletic clubs, landfills), the physical real estate assets are integral parts of an ongoing business. The market value of such a property (including all the tangible and intangible assets of the going concern, as if sold in aggregate) is commonly referred to by laymen as business value or business enterprise value, but in reality it is market value of the going concern including real property, personal property and the intangible assets of the business.
>
> Going concern value includes the incremental value associated with the business concern, which is distinct from the value of the tangible real property and personal property. The value of the going concern includes an intangible enhancement of the value of the operating business enterprise, which is produced by the assemblage of the land, buildings, labor, equipment and the marketing operations. Appraisal Institute, *The Appraisal of Real Estate*, (Chicago, 13th ed, 2008), pp 29, 30.

In *Amway Grand Plaza Hotel v City of Grand Rapids*, 2001 WL 1557496, (Mich. Tax Tribunal), November 26, 2001, MTT Docket No. 237807, the Tribunal found some merit in the Rushmore method. The court discussed the Rushmore method as follows (in pertinent excerpts):

> Business Value Adjustment
>
> Several procedures can be used to estimate the business value of a lodging facility. In the current economic environment, the most appropriate theory is to presume that a professional management agent is employed to take over the day-to-day operation of the hotel, thereby allowing the owner to maintain only a passive interest. Thus the income attributed to the business is taken by the managing agent in the form of a management fee. Deducting the management fee from the stabilized net income removes a portion of the business component from the income stream. An additional business value deduction must be made if the property benefits from a chain affiliation. This is accomplished by either increasing the management fee expense or making a separate franchise fee deduction. (pp 243-244).
>
> The explanation, however, is incomplete, a point of interest to the Tribunal. In understanding development of the going concern value under the Rushmore method, the cross-examination by Petitioner's attorney is enlightening (Tr of 3-17-99 pm, pp 162-163). An insightful segment of that testimony regarded the manner in which the method employed in tax assessment assignments would vary from another type of appraisal assignment--those requiring the going concern to remain intact (i.e., property and business combined). Note the answer relative to the full going concern valuation, and how it differs from his process for extracting real property under tax assessment assignments:

Q: What is the difference--is there any difference between what you value hotels which include real property, tangible personal property and intangible property from what you do here in a valuation for assessment purposes? Is there any difference between the two?

A: I would not deduct the income attributed to the personal property, return on personal property, and I would not deduct the management fee...or franchise fee.

As described in this exchange, the Rushmore method would make no income reductions for items providing business functions (personal property, management, franchise) if the assignment calls for the value of the entire hotel to be inclusive of all business enterprise components. The explanation offered is that the going concern net income will be higher in that there have been no deductions attributable to the business enterprise items. That difference is compared to an assignment for assessment purposes where only the value of the real property is desired. In that case, the business adjustment is a deduction of income reflected by Respondent's view of the business elements (personal property, management, franchise)--and the Tribunal adds the liquor licenses), leaving a lesser residual net income attributable to the real property (before property tax adjustment). What is troublesome to the Tribunal is, first, the manner in which income and expense terminology is being interchanged; second, Mr. Rushmore's procedural definition of the going concern excludes certain critical business expenses; and third, that while the real property extraction process does involve recognition of removal of business functions, the method still does not produce evidence that those functions do or do not result in a separate business value of their own. These matters are discussed following.

c. Development of the Going Concern Is Incomplete. As noted, Respondent's method is confusing in its concept since it effects business expense adjustments as if they were income items, a process untypical of standard appraisal methodology for the Income Approach format. That observation leads into the second issue, that the Tribunal finds Mr. Rushmore's development of the going concern valuation to be an incomplete process. The most obvious variation from standard appraisal methodology is the development of the going concern net income. Notice that it is identical in both illustrations, the first column corresponding to Mr. Rushmore's testimony under cross-examination (except that the Tribunal earlier found that the liquor licenses are also a business element, contrary to Mr. Rushmore's opinion). He testified that, in valuing only the going concern, he would not deduct the income attributable to the personal property, management fee, or franchise fee. That is exactly demonstrated by the first column and, in fact, is also demonstrated in the second column (pertaining to tax assessment work), where the procedure to develop the going concern value is identical. With that background, several areas of omission are noted.

Respondent's procedure begs the question, where is there an accounting of the business expense necessary to producing the income? Expenses provide the

functions of operation, which in turn generate going concern income, from which the expenses are paid and the net income realized--the circular process then repeating itself. Likewise, in Mr. Rushmore method, the going concern income is derived from an outlay of cash, that is, business expenses sufficient to acquire the management function, secure the benefits of the franchise affiliation, and realize the productivity of millions of dollars in personal property. Therefore, the question is asked again, where is the cost (the expense) of those functions accounted for, the cost of which produces the income from which Mr. Rushmore makes his deduction adjustments? The Tribunal has no issue with the fact that management, franchise and personal property comprise business functions, and agrees in concept that the measure of those functions is best determined by the funds exchanged in the marketplace between buyers and providers of those services. For example, if the standard charge for management of a small office shopping center was 5% of Effective Gross Income (EGI), and the EGI was $100,000 annually, then the yearly management fee would be 5% of $100,000 or $5,000. That would be the market price paid by buyers of the management services, and the price charged by providers of management services to produce the effective gross income results. In this example, the business value influence of the business function of management is $100,000. If there is any business value relative to the shopping center, it would be confined to all or part of the 5% management fee, not part of the $100,000 EGI. The $100,000 of EGI is readily available to anyone for a mere 5% charge, and there is no reason, by the principle of substitution, for a market buyer to pay more than that fee to acquire income-generating management services. As viewed by the Tribunal, under this example, there is no business value resident within the hypothetical property, since all net income would be required to provide a market investment return on the real property. Had there been any business value, it would be extracted by the management company as part of the potential net income in the form of a 5% fee. In a general and simplified form, that is Mr. Rushmore's theory as the Tribunal interprets it.

Thus, using this simple example, Mr. Rushmore's theory is correct in a limited aspect, that the outlay for personal property, management and franchise affiliation, is a reasonable measure of the business functions. Whether those functions represent marketable business value or merely value influencers is uncertain, but neither is it critical to know the answer once the deduction is taken. However, the Tribunal finds that it is not gross income that is being removed, but a reduction in the net income of the going concern through a business expenditure. On that basis, the issue is that the elements described as “business adjustments” are actually better expressed as business expenses, and need to be deducted as part of finding the net income of the going concern. Applying the example to subject hotel, the Tribunal cannot accept as valid a process wherein the property generates revenue from value-influencing functions, but does so without expending funds to acquire those essential functions of management, franchise affiliation, and personal property. The Tribunal concludes that the Rushmore method of developing the going concern (meaning, inclusive of

property and business), is incompletely processed, and is flawed as to the failure to deduct management expenses for both the property and the business, the franchise fee, and the personal property replacement allowance as legitimate expenses of the going concern.

Business Functions Are Not Evidence of Business Value. The Tribunal takes no issue with Mr. Rushmore on that part of his theory regarding the management, franchise, and personal property as elements of the business being conducted on the real property of subject hotel. The Tribunal will acknowledge that the personal property and liquor license are business enterprise elements, each with their own separately marketable identity. What is not accepted in its entirety is that the management and franchise items represent business enterprise value, that is, a separately identifiable component recognized by the marketplace as possessing market value enhancement to the property. As already extensively discussed, there is no market evidence of any business value included in the hotel sales data. What Respondent is describing as business value is really a business expense that generates business functions that are, under Michigan law, properly classified as value influencers. After deduction of personal property and the liquor licenses, there is an absence of any other clearly business enterprise elements not already properly classified as value influencers.

Mr. Rushmore method, as discussed in the preceding paragraph, after adjustment for inclusion of proper expenses of the going concern, neither produces a residual income of the business, nor is there any market evidence of its existence. Interestingly, Respondent's appraisers found no residual business net income of the going concern, and neither does the Tribunal under its reasoning and findings. Respondent's theory does state that any business value is removed by removal of income attributable to the management, franchise, and personal property expenses. In that regard, Respondent’s method has merit--but for the wrong reasons. The management and franchise functions are more properly considered as expenses of the going concern, whose contribution to the real property is as value-influencers. They may or may not also include some business enterprise value, but that is not material once the business expense (or business income, as Respondent terms it), is deducted, taking with its deduction whatever elements comprise the expense's subtract from, and diminishment of, net income. As to the personal property (to which the Tribunal has added the liquor licenses), Respondent's deduction of that contribution, being an independently identifiable and marketable element, is not in dispute as a proper business deduction. Petitioner also deducts that asset from the going concern, as does the Tribunal. Parts of that deduction are business property, parts may be necessary to operation of the real property, but the exact identification of function is not material, since the personal property is also being deducted because it is tangible property of the going concern, already taxed.

The Tribunal finds that in the instant case Petitioner's allocation of Non-Assessables (P-1, p 79) does not have a market basis upon which a $500,000 deduction should be made to the income approach.

Respondent did not explain how the Rushmore method was applied other than to extract the return on and of the personal property by capitalizing 4% of the reserves for replacement, and deducting income applicable to the personal property. The Tribunal finds this adjustment should not include a capitalization rate loaded for taxes, because the personal property pays property taxes separately. The capitalization of both 4% of the reserves and the actual personal property are a double deduction. The Tribunal, when considering both parties' income and expenses, finds that they are very close with some minor adjustments, and finds that the true cash value of subject property is calculated using $55.14 average daily rate multiplied by 130 rooms multiplied by 365 days $2,616,393 gross income. Market occupancy of 64.8% is utilized for an effective gross income of $1,695,422. Both parties have expense ratios that are similar. Petitioner's expense ratio is 72.67%; Respondent's expense ratio (after the deduction of income imputable to the personal property) is 72.24%. The 72.24% is multiplied by the effective gross income of $1,695,422 for expensed to be deducted of 41,224,772 for a net operating income of $470,650. The final step is to capitalize the net operating income by dividing it by the tax neutral capitalization rate. Petitioner documented the origin of the capitalization rate of 9.750. The effective tax rate (without administration fee) of 2.869 is added for an overall capitalization rate of 12.619. The net operating income of $470,650 is divided by .12619 to result in a true cash value of $3,729,693 rounded to $3,730,000. This calculation appears below:

$55.14 ADR X 130 X 365 days =	$2,616,393
64.8% occupancy=	

Effective Gross Income (EGI) $1,695,422
Expenses 72.24% of EGI $1,224,772
EGI minus expenses for Net operating income (NOI)
NOI $470,650
NOI divided by Capitalization Rate for TCV
$470,650 divided by .12619 $3,729,693

Therefore, the Tribunal finds the following values for the subject property for tax year 2006:

PARCEL #	TCV	SEV	TV
80-043-99-0005-001	$3,730,000	$1,865,000	$1,865,000

Conclusions of Law

The assessment of real property in Michigan is governed by the constitutional standard that property shall not be assessed in excess of 50% of its true cash value, as equalized, and that beginning in 1995 the taxable value is limited by statutorily determined general price increases, adjusted for additions and losses.

A proceeding before the Tax Tribunal is original, independent, and de novo. MCL 205.735(1). The Tribunal's factual findings are to be supported by competent, material, and substantial evidence. *Antisdale v City of Galesburg*, 420 Mich 265, 277; 362 NW2d 632 (1984); *Dow Chemical Co v Dept of Treasury*, 185 Mich App 458, 462-463; 452 NW2d 765 (1990). "Substantial evidence must be more than a scintilla of evidence, although it may be substantially less than a preponderance of the evidence." (Citations omitted) *Jones & Laughlin Steel Corp v City of Warren*, 193 Mich App 348, 352-353; 483 NW2d 416 (1992).

As used in the General Property Tax Act, "true cash value" means the usual selling price at the place where the property to which the term is applied is at the time of assessment, being the price

that could be obtained for the property at private sale, and not at auction sale except as otherwise provided in this section, or at forced sale. MCL 211.27(1).

"True cash value" is synonymous with "fair market value." *CAF Investment Co v State Tax Comm*, 392 Mich 442, 450; 221 NW2d 588 (1974). The Michigan Supreme Court, in *Meadowlanes, supra*, acknowledged that the goal of the assessment process is to determine "the usual selling price for a given piece of property." In determining a property's true cash value or fair market value, Michigan courts and the Tribunal recognize the three traditional valuation approaches as reliable evidence of value. See *Antisdale v Galesburg*, *supra*.

"The petitioner has the burden of establishing the true cash value of the property...." MCL 205.737(3); MCL 211.27(1); *Meadowlands Limited Dividend Housing Ass'n v City of Holland*, 437 Mich 473, 483-484; 473 NW2d 363 (1991). "This burden encompasses two separate concepts: (1) the burden persuasion, which does not shift during the course of the hearing; and (2) the burden of going forward with the evidence, which may shift to the opposing party." *Jones & Laughlin, supra* at 354-355, citing: *Kar v Hogan*, 399 Mich 529, 539-540; 251 NW2d 77(1976); *Holy Spirit Ass'n for the Unification of World Christianity v Dept of Treasury*, 131 Mich App 743, 752; 347 NW2d 707(1984).

The three most common approaches to valuation are the capitalization of income approach, the sales comparison or market approach, and the cost-less-depreciation approach. *Meadowlanes*, at 484-485; *Pantilind Hotel Co v State Tax Comm*, 3 Mich App 170; 141 NW2d 699 (1966), aff'd 380 Mich 390 (1968); *Antisdale*, at 276. The Tribunal is under a duty to apply its own expertise

to the facts of the case to determine the appropriate method of arriving at the true cash value of the property, utilizing an approach that provides the most accurate valuation under the circumstances. *Antisdale*, at 277.

Under MCL 205.737(1), the Tribunal must find a property's true cash value in determining a lawful property assessment. *Alhi Development Co v Orion Twp*, 110 Mich App 764, 767; 314 NW2d 479 (1981). The Tribunal may not automatically accept a respondent's assessment but must make its own finding of fact and arrive at a legally supportable true cash value. *Pinelake Housing Cooperative v Ann Arbor*, 159 Mich App 208, 220; 406 NW2d 832 (1987); *Consolidated Aluminum Corp v Richmond Twp*, 88 Mich App 229, 232-233; 276 NW2d 566 (1979). The Tribunal is not bound to accept either of the parties' theories of valuation. *Teledyne Continental Motors v Muskegon Twp*, 145 Mich App 749, 754; 377 NW2d 908 (1985). The Tribunal may accept one theory and reject the other, it may reject both theories, or it may utilize a combination of both in arriving at its determination. *Meadowlanes*, at 485-486; *Wolverine Tower Associates v City of Ann Arbor*, 96 Mich App 780; 293 NW2d 669 (1980); *Tatham v City of Birmingham*, 119 Mich App 583, 597; 326 NW2d 568 (1982).

In this case, the Tribunal concludes that the evidence, testimony and law favor the application of the income approach. An appraisal of fair market value requires a determination of the property's "highest and best use," which is "the reasonably probable and legal use of vacant land or an improved property that is legally permissible, physically possible, financially feasible, and that results in the highest value." Appraisal Institute, *Appraising Residential Properties*, (Chicago, 3rd ed., 1999, p 211).

The Tribunal concludes that neither party's appraisal is entirely persuasive. The Tribunal finds that an independent determination of the true cash value of subject property results in a slight increase in the true cash value and no adjustment for the taxable value.

JUDGMENT

IT IS ORDERED that the property's assessed and taxable values for the 2006 tax year shall be as set forth in this Final Opinion and Judgment.

IT IS FURTHER ORDERED that the officer charged with maintaining the assessment rolls for the tax years at issue shall correct or cause the assessment rolls to be corrected to reflect the property's true cash and taxable values as finally shown in this Final Opinion and Judgment within 20 days of the entry of the Final Opinion and Judgment, subject to the processes of equalization. See MCL 205.755. To the extent that the final level of assessment for a given year has not yet been determined and published, the assessment rolls shall be corrected once the final level is published or becomes known.

IT IS FURTHER ORDERED that the officer charged with collecting or refunding the affected taxes shall collect taxes and any applicable interest or issue a refund as required by the Final Opinion and Judgment within 28 days of the entry of the Final Opinion and Judgment. If a refund is warranted, it shall include a proportionate share of any property tax administration fees paid and of penalty and interest paid on delinquent taxes. The refund shall also separately indicate the amount of the taxes, fees, penalties, and interest being refunded. A sum determined by the Tribunal to have been unlawfully paid shall bear interest from the date of payment to the

date of judgment and the judgment shall bear interest to the date of its payment. A sum determined by the Tribunal to have been underpaid shall not bear interest for any time period prior to 28 days after the issuance of this Final Opinion and Judgment. Pursuant to MCL 205.737, interest shall accrue (i) after December 31, 1995, at a rate of 6.55% for calendar year 1996, (ii) after December 31, 1996, at a rate of 6.11% for calendar year 1997, (iii) after December 31, 1997, at a rate of 6.04% for calendar year 1998, (iv) after December 31, 1998, at the rate of 6.01% for calendar year 1999, (v) after December 31, 1999, at the rate of 5.49% for calendar year 2000, (vi) after December 31, 2000, at the rate of 6.56% for calendar year 2001, (vii) after December 31, 2001, at the rate of 5.56% for calendar year 2002, (viii) after December 31, 2002 at the rate of 2.78% for calendar year 2003, (ix) after December 31, 2003, at the rate of 2.16% for calendar year 2004, (x) after December 31, 2004, at the rate of 2.07% for calendar year 2005, (xi) after December 31, 2005, at the rate of 3.66% for calendar year 2006, (xii) after December 31, 2006, at the rate of 5.42% for calendar year 2007, and (xiii) after December 31, 2007, at the rate of 5.81% for calendar year 2008, and (xiv) after December 31, 2008, at the rate of 3.31% for calendar year 2009.

This Order resolves all pending claims in this matter and closes this case.

MICHIGAN TAX TRIBUNAL

Entered: September 29, 2009 By: Victoria L. Enyart