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THE TAX COURT COMMITTEE ON OPINIONS

TAX COURT OF NEW JERSEY

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Presiding Judge

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Re: J M R & R Associates v. Borough of Manville
Docket No. 007861-2010
Docket No. 007260-2011
Docket No. 003335-2012

Dear Counsel:

This letter constitutes the court's opinion after trial in the above-referenced matters challenging the local property tax assessment on plaintiff's real property for tax years 2010, 2011 and 2012. For the reasons stated more fully below, the assessment for each year is reduced.

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I. Procedural History and Findings of Fact

The following findings of fact and conclusions of law are based on the evidence and testimony admitted at trial.

Plaintiff J M R & R Associates is the owner of real property in defendant Manville Borough. The property is designated in the records of the municipality as Block 220, Lot 1 and is commonly known as 440 So. Main Street.

For tax years 2010, 2011, and 2012, the subject property was assessed as follows:

Land	$ 285,000
Improvement	$ 840,000
Total	$1,125,000

For each of the tax years at issue, the average ratio for the municipality exceeded 100%.

Plaintiff filed timely Complaints in this court challenging the assessment for each of the tax years.

The subject property is unusual. It consists of two buildings in the town's central business district. One structure has 7,474 square feet of retail space, 1,350 square feet of auto repair space and four, second-story, residential rental apartments comprising 3,760 square feet of living space. The second building is a two-story apartment building which is situated behind the retail store and off of the main road with six two-bedroom apartments. The two buildings sit on .8 acres adjacent to a brook in a flood zone. In the past, the buildings have experienced vacancies related to flooding. The property experienced significant flooding in the aftermath of Tropical Storm Irene in 2011 resulting in a retail space vacancy of several months. There is sufficient parking for all of the uses, both on the street and on the property. The property generates rental income from each of its various uses.

The building containing retail space, car service space and apartments is unremarkable in its design, with a plain exterior fronting South Main Street. The building appears to be in fair condition. The structure containing only apartments is newer, although its exact age was not identified at trial. The building has a residential appearance with vinyl siding and is behind the retail building, shielding the residences from South Main Street. A fenced-in parking lot adjoins the apartment building.

The property is located in the municipality's "Industrial" zone. Permitted uses in the zone include plants for light manufacturing, fabricating, compounding, assembling, storage and other processing of commodities, materials or equipment. In addition, the zone permits research laboratories, executive and administrative offices, and employee education and training facilities. Plaintiff's use of the property on the relevant valuation dates was a grandfathered non-conforming use.

The taxpayer presented the testimony of an expert real estate appraiser. He opined that the current use of the property was its highest and best use on each of the valuation dates. To reach an opinion of value, the expert used the income approach, which is common for income-generating property. He offered an opinion of three separate economic rents for the subject: a monthly rent for the retail space, a monthly rent the car service area and monthly rents for the apartments, which he opined was the actual rents. The expert combined the rents from the three categories into a single income stream and applied a single vacancy rate to determine potential gross income. The expert then used actual expenses from the subject to determine net operating income for the property. He applied a single capitalization rate to convert his opinion of net operating income into an opinion of true market value for the entire parcel.

The expert offered the opinion that the subject property had a true market value of $858,000 on October 1, 2009; $856,000 on October 1, 2010; and $901,000 on October 1, 2011. These values are less than the assessments in each tax year and would warrant a reduction in the assessments if adopted by the court.

During trial the municipality moved to strike the expert's testimony as net opinion. In addition, at the close of plaintiff's case the municipality moved, in effect, for a directed verdict and to dismiss plaintiff's Complaints for failure to overcome the presumption of validity attached to the assessments. Those motions were denied. The borough did not present the testimony of an expert, electing instead to rely on its cross-examination of plaintiff's witness.

II. Conclusions of Law

The court's analysis begins with the well-established principle that "[o]riginal assessments . . . are entitled to a presumption of validity." MSGW Real Estate Fund, LLC v. Borough of Mountain Lakes, 18 N.J. Tax 364, 373 (Tax 1998). As Judge Kuskin explained, our Supreme Court has defined the parameters of the presumption as follows:

> The presumption attaches to the quantum of the tax assessment. Based on this presumption the appealing taxpayer has the burden of proving that the assessment is erroneous. The presumption in favor of the taxing authority can be rebutted only by cogent evidence, a proposition that has long been settled. The strength of the presumption is exemplified by the nature of the evidence that is required to overcome it. That evidence must be "definite, positive and certain in quality and quantity to overcome the presumption."

Ibid. (quoting Pantasote Co. v. City of Passaic, 100 N.J. 408, 413 (1985)(citations omitted)).

The presumption of correctness arises from the view "that in tax matters it is to be presumed that governmental authority has been exercised correctly and in accordance with law." Pantasote, supra, 100 N.J. at 413 (citing Powder Mill, I Assocs. v. Township of Hamilton, 3 N.J. Tax 439

(Tax 1981)); see also Byram Twp. v. Western World, Inc., 111 N.J. 222 (1988). The presumption remains "in place even if the municipality utilized a flawed valuation methodology, so long as the quantum of the assessment is not so far removed from the true value of the property or the method of assessment itself is so patently defective as to justify removal of the presumption of validity." Transcontinental Gas Pipe Line Corp. v. Township of Bernards, 111 N.J. 507, 517 (1988).

"The presumption of correctness . . . stands, until sufficient competent evidence to the contrary is adduced." Little Egg Harbor Twp. v. Bonsangue, 316 N.J. Super. 271, 285-86 (App. Div. 1998)(citation omitted); Atlantic City v. Ace Gaming, LLC, 23 N.J. Tax 70, 98 (Tax 2006). "In the absence of a R. 4:37-2(b) motion . . . the presumption of validity remains in the case through the close of all proofs." MSGW Real Estate Fund, LLC, supra, 18 N.J. Tax at 377. In making the determination of whether the presumption has been overcome, the court should weigh and analyze the evidence "as if a motion for judgment at the close of all the evidence had been made pursuant to R. 4:40-1 (whether or not the defendant or plaintiff actually so moves), employing the evidentiary standard applicable to such a motion." Ibid. The court must accept as true the proofs of the party challenging the assessment and accord that party all legitimate favorable inferences from that evidence. Id. at 376 (citing Brill v. Guardian Life Ins. Co. of Am., 142 N.J. 520, 535 (1995)). In order to overcome the presumption, the evidence "must be 'sufficient to determine the value of the property under appeal, thereby establishing the existence of a debatable question as to the correctness of the assessment.'" West Colonial Enters, LLC v. City of East Orange, 20 N.J. Tax 576, 579 (Tax 2003)(quoting Lenal Props., Inc. v. City of Jersey City, 18 N.J. Tax 405, 408 (Tax 1999), certif. denied, 165 N.J. 488 (2000)), aff'd, 18 N.J. Tax 658 (App. Div. 2004).

Only after the presumption is overcome with sufficient evidence at the close of trial must the court "appraise the testimony, make a determination of true value and fix the assessment."

Rodwood Gardens, Inc. v. City of Summit, 188 N.J. Super. 34, 38-39 (App. Div. 1982). If the court determines that sufficient evidence to overcome the presumption that the assessment is correct has not been produced, the assessment shall be affirmed and the court need not proceed to making an independent determination of value. Ford Motor Co. v. Township of Edison, 127 N.J. 290, 312 (1992); Global Terminal & Container Serv. v. City of Jersey City, 15 N.J. Tax 698, 703-04 (App. Div. 1996).

As explained at trial, the court concludes that plaintiff produced sufficient evidence to overcome the presumption of validity attached to the assessments. If taken as true, the opinion of plaintiff's expert and the facts upon which he relied, create a debatable question regarding the correctness of the assessment in each tax year sufficient to allow the court to make an independent determination of the value of plaintiff's property. The expert opined that on each valuation date the subject property was worth significantly less than the assessment for that year. As noted above, the average ratio for Manville Borough exceeds 100% for each tax year. Thus, if the property's true market value is below the assessment in any year, the property owner would be entitled to relief.

The court's inquiry, however, does not end here. Once the presumption is overcome, the "court must then turn to a consideration of the evidence adduced on behalf of both parties and conclude the matter based on a fair preponderance of the evidence." Ford Motor Co., supra, 127 N.J. at 312 (quotations omitted). "[A]lthough there may have been enough evidence to overcome the presumption of correctness at the close of plaintiff's case-in-chief, the burden of proof remain[s] on the taxpayer throughout the entire case . . . to demonstrate that the judgment under review was incorrect." Id. at 314-15 (citing Pantasote, supra, 100 N.J. at 413).

A. Highest and Best Use.

An essential element of the court's determination of the true market value of the subject property is a finding of the property's highest and best use. In his recent opinion in Clemente v. Township of South Hackensack, 27 N.J. Tax 255, 267-269 (Tax 2013), appeal pending, Judge Andresini succinctly explained the legal precedents that guide this court in making a highest and best use determination:

> For property tax assessment purposes, property must be valued at its highest and best use. Ford Motor Co. v. Township of Edison, 127 N.J. 290, 300-01, 604 A.2d 580 (1992). "Any parcel of land should be examined for all possible uses and that use which will yield the highest return should be selected." Inmar Associates, Inc. v. Township of Edison, 2 N.J. Tax 59, 64 (Tax 1980). Accordingly, the first step in the valuation process is the determination of the highest and best use for the subject property. American Cyanamid Co. v. Township of Wayne, 17 N.J. Tax 542, 550 (Tax 1998), aff'd, 19 N.J. Tax 46 (App. Div. 2000). "The concept of highest and best use is not only fundamental to valuation but is a crucial determination of market value. This is why it is the first and most important step in the valuation process." Ford Motor Co. v. Township of Edison, 10 N.J. Tax 153, 161 (Tax 1988), aff'd o.b. per curiam, 12 N.J. Tax 244 (App. Div. 1990), aff'd, 127 N.J. 290, 604 A.2d 580 (1992); see also Gen. Motors Corp. v. City of Linden, 22 N.J. Tax 95, 107 (Tax 2005).
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> The definition of highest and best use contained in The Appraisal of Real Estate, a text frequently used by this court as a source of basic appraisal principles, has remained relatively constant for all of the years under appeal. Highest and best use is defined as:
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> > The reasonably probable and legal use of vacant land or improved property that is physically possible, appropriately supported, and financially feasible and that results in the highest value.
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> > [Appraisal Institute, The Appraisal of Real Estate, 22 (13th ed. 2008).]
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> The highest and best use analysis requires sequential consideration of the following four criteria, determining whether the use of the

> subject property is: 1) legally permissible; 2) physically possible; 3) financially feasible; and 4) maximally productive. Ford Motor Co., supra, 10 N.J. Tax at 161; see also The Appraisal of Real Estate at 279. Implicit in this analysis is the assumption that the proposed use is market-driven; in other words, that it is determined in a value-in-exchange context and that there is a market for such use. WCI-Westinghouse v. Township of Edison, 7 N.J. Tax 610, 616-17 (Tax 1985), aff'd o.b. per curiam, 9 N.J. Tax 86 (App. Div. 1986). A highest and best use determination is not based on value-in-use because the determination is a function of property use and not a function of a particular owner's use or subjective judgment as to how a property should be used. See Entenmann's Inc. v. Borough of Totowa, 18 N.J. Tax 540, 545 (Tax 2000). The highest and best use of an improved property is the "use that maximizes an investment property's value, consistent with the rate of return and associated risk." Ford Motor Co., supra, 127 N.J. at 301, 604 A.2d 580. Further, the "actual use is a strong consideration" in the analysis. Ford Motor Co., supra, 10 N.J. Tax at 167.
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> Highest and best use is not determined through subjective analysis by the property owner. The Appraisal of Real Estate at 279. The proper highest and best use requires a comprehensive market analysis to ascertain the supply and demand characteristics of alternative uses. See Cherry Hill, Inc. v. Township of Cherry Hill, 7 N.J. Tax 120, 131 (Tax 1984), aff'd, 8 N.J. Tax 334 (App. Div. 1986). Additionally, the proposed use must not be remote, speculative, or conjectural. Id. If a party seeks to demonstrate that a property's highest and best use is other than its current use, it is incumbent upon that party to establish that proposition by a fair preponderance of the evidence. Penn's Grove Gardens, Ltd v. Borough of Penns Grove, 18 N.J. Tax 253, 263 (Tax 1999); Ford Motor Corp., supra, 10 N.J. Tax at 167. Property should be assessed in the condition in which it is utilized and the burden is on the person claiming otherwise to establish differently. Highview Estates v. Borough of Englewood Cliffs, 6 N.J. Tax 194, 200 (Tax 1983).

The highest and best use opinion offered by the taxpayer's expert is the use to which the property was put on the relevant valuation dates. It is, therefore, the burden of the municipality, which did not present an expert witness, to establish that the highest and best use of the subject property is some other purpose.

Although plaintiff's expert undertook no extensive market study with respect to the subject property's highest and best use, he credibly testified that no market existed in downtown Manville for the uses permitted in the Industrial zone. He testified that he is familiar with downtown Manville, having appraised many properties in the borough and nearby towns. The township has an established recent history of moving away from industrial uses that previously dominated the downtown area of the municipality. In addition, the location of the subject property in a flood zone in a largely retail and residential neighborhood renders office and light industrial uses remote possibilities for the subject. The municipality, which challenges the expert's identification of the current use as the highest and best use, offered no expert opinion to bolster its argument. It merely argues that plaintiff's expert's analysis on the point was insufficient.

As Judge Andresini explained, however, the determination of a property's highest and best use begins with the proposition that the property should be valued as it was used on the valuation date and the party proposing a different highest and best use bears the burden of producing evidence to support its position. Here, plaintiff's expert examined the current use of the property and, after applying his experience as an appraiser in the Manville area and his familiarity with the municipality, determined that the current use was the property's highest and best use. The court finds the expert's opinion on this point to be credible. Having produced no evidence suggesting that any other use of the subject would satisfy the criteria for a finding of highest and best use, the municipality has not undermined the credibility of the expert's opinion in this regard.

B. Approach to Valuation.

"There are three traditional appraisal methods utilized to predict what a willing buyer would pay a willing seller on a given date, applicable to different types of properties: the comparable sales method, capitalization of income and cost." Brown v. Borough of Glen Rock,

19 N.J. Tax 366, 376 (App. Div.)(citing Appraisal Institute, The Appraisal of Real Estate 81 (11th ed 2006)), certif. denied, 168 N.J. 291 (2001). "There is no single determinative approach to the valuation of real property." 125 Monitor Street, LLC v. City of Jersey City, 21 N.J. Tax 232, 237 (Tax 2004)(citing Samuel Hird & Sons, Inc. v. City of Garfield, 87 N.J. Super. 65, 72 (App. Div. 1965); ITT Continental Baking Co. v. Township of East Brunswick, 1 N.J. Tax 244 (Tax 1980)), aff'd, 23 N.J. Tax 9 (App. Div. 2005). "The choice of the predominate approach will depend upon the facts of each case and the reaction of the experts to those facts." Id. at 238 (citing City of New Brunswick v. Division of Tax Appeals, 39 N.J. 537 (1963); Pennwalt Corp. v. Township of Holmdel, 4 N.J. Tax 51, 61 (Tax 1982)).

Plaintiff's expert relied on the income approach to valuing the subject property. The income capitalization approach is the preferred method of estimating the value of income producing property. Parkway Village Apartments Co. v. Township of Cranford, 108 N.J. 266, 270 (1987); Hull Junction Holding Corp. v. Borough of Princeton, 16 N.J. Tax 68, 79 (Tax 1996). "In the income capitalization approach, an appraiser analyzes a property's capacity to generate future benefits and capitalizes the income into an indication of present value." Appraisal Institute, The Appraisal of Real Estate 445 (13th ed 2008). The court finds that the income capitalization approach is the best method for determining the value of the subject property, which produces income from a variety of uses.

The court notes that plaintiff's expert did not apply different approaches to value to different elements of the subject property. This court has recognized a valuation methodology of this type may be appropriate in some circumstances. See Livingston Mall Corp. v. Township of Livingston, 15 N.J. Tax 505, 508-09 (Tax 1996)(applying cost approach to determine value of anchor stores and income approach to determine value of non-anchor stores in same mall property). Plaintiff's

expert used only one approach – the income approach – to reach an opinion as to the true market value of the subject property. He did, however, opine three different market rents for the subject – one for each of the three uses to which the property is put. The court concludes that the expert's approach is sensible, given the distinct types of rental spaces at the property. The court concludes that it is credible that a buyer and seller of the subject property would anticipate varying market rents for the various areas of the subject property which generate rental income.

C. Calculation of Value Using Income Approach.

Determining the value of real property pursuant to the income approach can be summarized as follows:

	Market Rent
x	Square Footage
	Potential Gross Income
-	Vacancy and Collection Losses
	Effective Gross Income
-	Operating Expenses
	Net Operating Income
÷	Capitalization Rate
	Value of Property

See Spiegel v. Town of Harrison, 19 N.J. Tax 291, 295 (App. Div. 2001), aff'g, 18 N.J. Tax 416 (Tax 1999); Appraisal Institute, The Appraisal of Real Estate 466 (13th ed 2008).

1. Market Rent.

"Central to an income analysis is the determination of the economic rent, also known as the 'market rent' or 'fair rental value.'" Parkway Village Apartments, supra, 108 N.J. at 270. This differs from the actual rental income realized on the property, which may be below market rates. Parkview Village Assocs. v. Borough of Collingswood, 62 N.J. 21, 29-30 (1972). However, actual income is a significant probative factor in the inquiry as to economic income. Id. at 30. "Checking

actual income to determine whether it reflects economic income is a process of sound appraisal judgment applied to rentals currently being charged for comparable facilities in the competitive area." Ibid.

Plaintiff's expert identified a separate market rent for each of the three types of rental spaces at the subject property.

(a) The Residential Apartments Economic Rent.

Plaintiff's expert used the actual income from the rental of the residential units at the subject property as economic rent. He did so based on his opinion that the subject property was well managed on the relevant valuation dates. This approach to determining market rent has its origin in the Supreme Court's holding in Parkview Village Assocs. In that case, the taxpayers challenged the assessments on four apartment buildings. All experts agreed that the income approach to valuation was the appropriate method for determining the true market value of the properties. The parties' experts offered competing views of fair market, or economic, rent for the properties and whether actual rents at the properties represented economic rents. After consideration of the competing evidence, the court established a general rule for determining economic rent:

> In the absence of convincing evidence to the contrary the current ongoing income scale of a large, well-managed apartment project like this, functioning as customary with leases of relatively short length, should be deemed prima facie to represent its fair rental value for purposes of the capitalized income method of property valuation. A court or taxing agency should be most hesitant to find that the tenants of a residential property being operated commercially are being charged inadequate rent. That approach, we believe, conduces to the objective of relative stability of assessments which we have heretofore held to be basic to sound tax assessment policy. Readily to be distinguished is the case of a taxpayer owning commercial property tied to a long term lease made long before the

> current assessing date, where the present rent may well be out of line with current fair rental value.
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> [62 N.J. at 34-35 (citations omitted).]

The Parkview presumption was reaffirmed by the Supreme Court in Parkway Village Apartments. In that case, the owner of a large, well-managed apartment complex with one-year leases challenged the assessment on the property. The income approach was used to determine true market value. The taxpayer's expert, relying on the holding in Parkview Village Assocs. testified that the actual rent charged for the apartments should be accepted as economic rent. The municipality's expert imputed to all apartments on the property the most recent rent charged for an apartment of that type. The most recent rent for each apartment type was higher than the actual rent for some apartments. Id. at 269.

The Court explained that the holding in Parkview Village Assocs. "was based on the belief that landlords of well-managed apartment complexes maximize their profits and minimize their expenses." Id. at 271. The court also noted that the holding in Parkview Village Assocs. had "been consistently followed." Ibid. (citing Glen Wall Assocs. v. Township of Wall, 99 N.J. 265, 275-76 (1985)). After reviewing several opinions in which the Parkview Village Assocs. holding had been applied, the Court held that "[w]e reaffirm the Parkview rule that in the absence of convincing evidence to the contrary, the actual rent of a well-managed apartment complex functioning with customary leases of relatively short length is prima facie representative of economic rent for the purpose of capitalized income of property valuation." Id. at 276.[1]

[1] The Parkview Village Assocs. rule was extended to hotel properties in Glen Pointe Assocs. v. Township of Teaneck, 10 N.J. Tax 380 (1989), aff'd, 12 N.J. Tax 118 (App. Div.), certif. denied, 122 N.J. 391 (1990).

Plaintiff's expert testified that the residential units at the subject property, although relatively few in number, are well managed. He therefore applied the Parkview Village Assocs. presumption that the rents generated by the residential units reflect economic rent for the residential units. The municipality contends that the subject property is not a large apartment complex, thus negating the Parkview Village Assocs. presumption. The borough cited no published legal precedent establishing a numerical limit on the number of residential units which must be present on a parcel for the Parkview Village Assocs. presumption to apply. The court detects no reason why the owner of the subject property, which has ten residential units available for rent, should not be presumed to be operating the property to maximize income and minimize expenses. The municipality offered no evidence that the taxpayer was charging below market rents for the residential units or incurring unusually high expenses. The fact that the property has a small number of units as compared to a larger apartment complex, standing alone, is an insufficient basis to depart from the holding in Parkview Village Assocs. Absent some evidence suggesting poor management, the court declines the municipality's invitation to reject the presumption of good management in this case.[2]

[2] Defendant's cross-examination of plaintiff's expert suggested that the property may not be well managed because the evidence suggests that residential rents were not increased during the tax years in question. Plaintiff's expert credibly testified that the residential units at the subject, above and behind main street retail units, adjacent to a car service facility, and in a flood zone, are not likely to attract tenants who can easily absorb frequent rent increases. Without some evidence to the contrary, the court accepts that the stability of the rents for the subject's residential units is consistent with good management of the subject property. Plaintiff's expert also examined six comparable residential leases in an effort to corroborate his opinion that the residential rents at the subject were market rents. The expert did not have a command of many important details with respect to the comparable apartment leases. The court gives no weight to the expert's testimony with respect to comparable apartment leases.

The court, therefore, accepts the opinion of plaintiff's expert that actual rents for the residential units at the subject property constitute economic rent.

(b) The Retail Space Economic Rent.

To formulate an opinion of economic rent for the retail spaces, plaintiff's expert examined six comparable retails leases. Two of the leases are for retail space in Manville. The remainder are for retail space in neighboring Somerset County municipalities. The leases ranged in date from September 2008 to June 2010.

The unadjusted rent in the six comparable retail leases ranged from $9.86 per square foot to $16.70 per square foot. The expert applied only a negative 10% location adjustment to five of the leases. He opined that the subject property's location was inferior to the comparable retail leases because of the subject property's adjacency to the Royce Brook. As is noted above, the subject property experiences periodic flooding, which has been severe enough to result in vacancies for as long as two months. The one comparable retail lease for which no location adjustment was made is also located on Main Street in Manville, although it is not entirely clear from the record whether the portion of Main Street on which the comparable retail lease is located is subject to flooding.

The expert offered the opinion that a time adjustment was not necessary for any of the comparable retail leases because rental rates for retail spaces of the type at the subject property were stable from 2008 through 2011. In addition, the expert testified that the comparable retail leases concerned buildings that were similar in type and condition to the subject and that no further adjustments were warranted.

The adjusted rents in the six comparable retail leases ranged from $6.82 per square foot to $15.03 per square foot. The expert considered these adjusted rental rates, along with two retail

leases at the subject property, one of which had an average rent of $8.95 per square foot over a five-year period and one of which had a rent of $5.19 per square foot. He concluded an economic retail rent of $10.00 per square foot for each of the valuation dates. This rate exceeds the rent in place at the subject property under the two subject leases considered by the expert.

The municipality's cross-examination of plaintiff's expert revealed some shortcomings in his analysis. The expert did not review all of the leases, relying instead in some instances in multiple listing information. In addition, the expert's opinion that no time adjustment was necessary was based on the subject retail leases and comparable retail leases and not on a fuller market analysis. In addition, the expert did not make an adjustment to one comparable retail lease for space in a suburban strip mall and not on a main street in a central business district, like the subject. Finally, the expert conceded that the retail comparable leases are not at mixed-use properties. While these points are meaningful, they do not, even when considered collectively, undermine the credibility of the expert's opinion to the point that it will be rejected by the court. The court accepts the expert's opinion with respect to economic retail rent for the subject.

(c) The Car Service Area Economic Rent.

In order to formulate an opinion with respect to the economic rent for the car service area, plaintiff's expert examined six comparable leases. Three of the six leases are for car service facilities in Somerset County. The three others are from out of the subject's county. The expert testified that it was necessary for him to expand his search beyond the subject's county because of the relative few number of such leases.

The unadjusted rents on the six comparable car service leases ranged from $7.85 per square foot to $23.28 per square foot. The expert applied two categories of adjustments. The first was an adjustment for location. The expert opined that the subject's location was inferior to each of

the comparable car services leases, given both the average location with respect to visibility, accessibility and traffic at the subject and the history of flooding. For this category the expert made a negative 10% adjustment for the three car service comparable leases in Somerset County and one of the out-of-county leases and a negative 20% for two car service leases in Montville, Morris County. The expert's explanation for the larger adjustments for the Morris County car service leases lacked credibility. He testified that he made larger adjustments for these comparable leases because property in Morris County generally has a higher value than property in Somerset County. This explanation does not address the crux of a location adjustment: a comparison of the characteristics of the subject property and the comparable property that may have an impact on rent. The court accepts only the negative 10% adjustments and will not rely on the two comparable car service leases from Morris County.

The second adjustment made by the expert to the car service comparable leases was for the structure of the comparable leases. The car service lease at the subject is on a modified gross basis, meaning that the landlord is responsible for local property taxes. Three of the car service comparable leases are on a triple net basis, meaning that the tenant is responsible for local property taxes. Naturally, the base rent on a triple net lease is less than it would be on a modified gross lease because the tenant in a triple net lease is also paying local property taxes. The expert made a positive 15% adjustment to the comparable leases to account for this difference. He did not, however, provide a credible explanation for this adjustment. The expert testified that he did not know the amount of local taxes paid by any of the tenants in the comparable car service leases. It is apparent that such amounts could readily be calculated and would provide a precise adjustment for this category. An across-the-board 15% adjustment in a category that could be determined

with precision lacks credibility. The court, therefore, will not rely on the three car service leases for which this adjustment was made.

Eliminating the two Morris County leases with large location adjustments (leases four and five) and the three leases with the structure adjustments (leases one, five and six), leaves the court with the two comparable car services leases from North Plainfield in Somerset County (leases two and three). These leases have adjusted rents of $11.51 and $13.97. The expert opined an economic rent of $13.50 for each of the valuation dates. This falls at the top end of this range. The court accepts this opinion as credible.[3]

2. Building Size.

There is no dispute with respect to the amount of rentable space at the subject property, the details of which are set forth above.

3. Vacancy and Collection Rate.

Plaintiff's expert opined a 10% factor for vacancy and collection loss. Although not stated in his report, the expert explained during his testimony that he relied on Korpacz, a national reporting service frequently relied upon by experts in the appraisal industry, to formulate his opinion. According to the expert, vacancies for properties less than investment grade, which is the case with the subject property, ranged from 2% to 15%. He opined a 10% vacancy and collection rate because the property is mixed use, experienced vacancies because of flooding, and had a vacant retail space for two years. In the absence of any meaningful evidence to the contrary, the court adopts the vacancy and collection rate offered by plaintiff's expert.

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[3] At trial, the municipality moved to strike car service comparable leases one, four, five and six because of the large size of the expert's proposed total gross adjustments. The court reserved on the motion. Because the court has decided not to rely on those leases for the reasons stated above, it is not necessary to decide defendant's motion.

4. Operating Expenses.

In keeping with his opinion that the subject property was well managed, plaintiff's expert relied on the actual expenses associated with the subject property for the period 2007 through 2010. After examining the taxpayer's records, the expert stabilized the actual expenses. He also opined a stabilized reserve for structural repairs and for the periodic replacement of appliances in the residential units. The expert opined a total of expenses and reserves of 39.5% of gross potential income. The municipality's cross-examination did not undermine the credibility of the expert's opinion in any meaningful way. The court, therefore, adopts the expert's opinion regarding expenses and reserves.

5. Capitalization Rate.

The overall capitalization rate is an "income rate for a total real property interest that reflects the relationship between a single year's net operating income expectancy and the total property price or value . . . ." Appraisal Institute, The Appraisal of Real Estate at 462. The overall capitalization rate is "used to convert net operating income into an indication of overall property value." Ibid.

Plaintiff's expert used the Band of Investment technique to calculate an overall capitalization rate. "This technique is a form of 'direct capitalization' which is used 'to convert a single year's income estimate into a value indication.' The technique includes both a mortgage and an equity component." Hull Junction Holding, supra, 16 N.J. Tax. at 80-81 (quoting Appraisal Institute, Appraisal of Real Estate 467 (10th ed 1992)).

> Because most properties are purchased with debt and equity capital, the overall capitalization rate must satisfy the market return requirements of both investment positions. Lenders must anticipate receiving a competitive interest rate commensurate with the perceived risk of the investment or they will not make funds

> available. Lenders generally require that the loan principal be repaid through periodic amortization payments. Similarly, equity investors must anticipate receiving a competitive equity cash return commensurate with the perceived risk, or they will invest their funds elsewhere.
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> [Appraisal Institute, Appraisal of Real Estate 505 (13th ed 2008).]

In "using the Band of Investment technique, it is incumbent upon the appraiser to support the various components of the capitalization rate analysis by furnishing 'reliable market data . . . to the court as the basis for the expert's opinion so that the court may evaluate the opinion.'" Hull Junction Holding, supra, 16 N.J. Tax at 82 (quoting Glen Wall Assocs., supra, 99 N.J. at 279-80). "For these purposes, the Tax Court has accepted, and the Supreme Court has sanctioned, the use of data collected and published by the American Council of Life Insurance." Id. at 82-83. "Relevant data is also collected and published by . . . Korpacz Real Estate Investor Survey." Id. at 83. "By analyzing this data in toto, the court can make a reasoned determination as to the accuracy and reliability of the mortgage interest rates, mortgage constants, loan-to-value ratios, and equity dividend rates used by the appraisers." Ibid.

The appropriate capitalization rate was a subject of contention at trial. Plaintiff's expert relied on reported capitalization data for retail properties. He did not examine capitalization rates for apartments or for mixed-use properties. He offered the opinion that insufficient data existed concerning mixed-use properties, that data concerning retail transactions would provide a credible range of rates for the subject property, and that he could consider the subject property's unusual characteristics when opining a capitalization rate from that range. The expert testified that capitalization data for apartment buildings would not be useful here because that data concerns large apartment complexes which are attractive to large investors. The subject property, by contrast, is below investment grade. In addition, the expert testified that the data concerning mixed

use properties was too slim to be reliable, given that the data related to only four transactions. From the data the expert determined to be credible he opined capitalization rates of 9.5% for tax year 2010, 9.6% for tax year 2011 and 9.0% for tax year 2012.

The court finds the expert's opinion with respect to the appropriate capitalization rates to be credible. The subject property is unusual. It is not surprising that no compilation of data exists with respect to properties that have the same characteristics as the subject. The expert took credible steps to identify a capitalization rate for the subject from existing data. In the absence of any competing data that represents a more credible opinion, the court adopts the capitalization rates of plaintiff's expert.

6. Calculation of Value.

Having accepted as credible the income, expenses and capitalization rate offered by plaintiff's expert, the court need not set forth at length the calculation of value for the subject property. Given that the court accepts as credible each of the components of the analysis of plaintiff's expert, the court also accepts the expert's value conclusions. The court, therefore, concludes that the true market value of the subject property is as follows:

For tax year 2010, the true market value of the subject property as of October 1, 2009 was $858,000.

For tax year 2011, the true market value of the subject property as of October 1, 2010 was $856,000.

For tax year 2012, the true market value of the subject property as of October 1, 2011 was $901,000.

C. Applying Chapter 123.

Pursuant to N.J.S.A. 54:51A-6(c), commonly known as Chapter 123, when the ratio of the assessed value of the subject property to its true value and the municipality's average ratio both exceed the county percentage (100%), the assessment must be reduced to reflect true value. This is the case here.

The formula for determining the subject property's ratio is:

Assessment ÷ True Value = Ratio

Here, that equation is represented as follows:

Tax Year 2010	$1,125,000	÷	$858,000	=	1.311
Tax Year 2011	$1,125,000	÷	$856,000	=	1.314
Tax Year 2012	$1,125,000	÷	$901,000	=	1.249

The ratio of the assessed value of the subject property to its true value exceeds 100% in each tax year. In addition, the average ratio for the municipality exceeded 100% in each of the tax years. The assessments for the subject property must, therefore, be reduced to reflect true value.

A Judgment establishing the assessment for the subject property for tax year 2010 will be entered as follows:

Land	$285,000
Improvement	$573,000
Total	$858,000

A Judgment establishing the assessment for the subject property for tax year 2011 will be entered as follows:

Land	$285,000
Improvement	$571,000
Total	$856,000

A Judgment establishing the assessment for the subject property for tax year 2012 will be entered as follows:

Land	$285,000
Improvement	$616,000
Total	$901,000

Very truly yours,

Patrick DeAlmeida, P.J.T.C.