BEFORE THE MONTANA TAX APPEAL BOARD

ABBEY/LAND LLC, Appellant, -vs- THE DEPARTMENT OF REVENUE OF THE STATE OF MONTANA, Respondent.	DOCKET NO.: PT-2013-12 FINDINGS OF FACT, CONCLUSIONS OF LAW, ORDER and OPPORTUNITY FOR JUDICIAL REVIEW

Statement of Case

Abbey/Land LLC (Taxpayer) appealed a decision of the Lake County Tax Appeal Board (CTAB) relating to the DOR's valuation of the improvements located on Shelter Island in Rollins, Montana. The Taxpayer argued at the CTAB hearing that the DOR overvalued both land and improvements for tax purposes and sought a reduction in the total value assigned by the DOR for tax year 2012. The CTAB affirmed the DOR values for the land at $3,715,785 and the improvements at $41,842,255. *See* ¶¶ 13-16. Taxpayer timely appealed the CTAB decision to this Board pursuant to §15-2-301, MCA. On appeal to this Board, Taxpayer did not contest the value assigned for the land, but sought a value of $9.8 million for the improvements.

The Shelter Island property in question sits on a 13.48-acre portion of a 24-acre private island in Flathead Lake. The main house was constructed over nearly a decade. It is one of finest houses ever built in Montana. The house has walls made of custom two-feet-thick stone blocks, custom-made glass windows, custom-made light fixtures, African mahogany paneling and cabinets, Italian plaster ceilings, floors made of imported Vietnamese marble, a roof made of blue Virginia slate roofing tiles with copper trim, and floors made of limestone tile. It has stone and copper exterior, and spans 19,452 square feet, with five bedrooms and eight bathrooms. *See* property record card; Ex. 13 ABBEY-DOR 000037-000040. The main residence has high ceilings, with the highest being about 45-feet. Each room has its own special architectural touches, fine finishes, and unusual lighting fixtures. The fireplace in the great room is made of limestone and there is a copper and glass conservatory, with a glass sky light at one end of the main floor. The main house has a custom kitchen with granite countertops, built-in commercial refrigerator, commercial freezers and other commercial appliances, along with a breakfast nook overlooking the lake, as well as a seating area and fireplace. Outside the home are a portico and 10,000 square feet of heated terrace and outdoor entertaining space. Some of the luxury amenities include a wine cellar, a state-of-the-art gym, sporting clay course, a dive shop, commercial computer-controlled HVAC systems in both homes, generator buildings, docks and seawalls. The

guesthouse spans 2,564 square feet and has two bedrooms and four bathrooms. The guesthouse doubles as a boathouse, which has a boat-capturing system, two boat-docking systems with automated boat retrieval systems (which pulls the boats into the main house or the guesthouse) and an underground shooting range. *See* Ex. 21; See also Ex. 1.

This Board considers the question of market value of the improvements *de novo*. *Montana Dep't of Revenue v. Burlington N. Inc.*, 169 Mont. 202, 545 P.2d 1083 (1976); *CHS, Inc. v. Montana Dep't of Revenue*, 2013 MT 100, 369 Mont. 505, 299 P.3d 813; *PacifiCorp v. Montana Dep't of revenue*, 2011 MT 93, 360 Mont. 259, 253 P.3d 847. The Board incorporated the appeal record from Lake County, admitted various pre-trial and post-trial filings, and stipulated exhibits. The Board also considered nearly twenty hours of the testimony and exhibits presented at the hearing.

The Montana Tax Appeal Board (Board) hearing was held November 17 through November 19, 2014, in Helena. Attorneys Milton Datsopoulos, William K. VanCanagan, and J. R. Casillas represented Taxpayer. Property owner Abbey/Land LLC member Donald G. Abbey, and expert witnesses Joseph R. Crosby, Dr. John R. Smith, Thomas G. Stevens, Malcolm Swan, and Gregory Thornquist all provided testimony and evidence in support of the appeal. Tax Counsels Daniel J. Whyte and Michele R. Crepeau represented the

Montana Department of Revenue (DOR.) DOR Appraiser Don Leuty, and DOR Region One Manager Scott Williams testified in support of the DOR value. DOR expert witnesses Richard Hagar and Graham Albertini presented testimony and evidence in opposition to the appraisal report prepared by the Taxpayer's expert witness Stevens. The record remained open to receive post-hearing briefs. On December 9, 2014, the record was closed.

Two new members were appointed to the Board on January 5, 2015. Both have reviewed the complete record. They are signing this opinion pursuant to the authority granted under §15-2-301(2), MCA. Therefore, this Board having fully considered the testimony, exhibits, post-hearing briefs, and all matters presented, finds and concludes the following:

Issue

The issue before this Board is whether the Department of Revenue determined an appropriate market value for the subject improvements for tax year 2012. The DOR's assessment of the land is not in dispute.

Summary

Abbey/Land LLC (Abbey) is the Taxpayer in this action and therefore bears the burden of proof. Based on a preponderance of the evidence, the Board modifies the depreciation factor and otherwise affirms the value DOR set for the improvements.

Evidence Presented

1. Due, proper and sufficient notice was given of this matter and of the time and place of the hearing. All parties had an opportunity to present both verbal and documentary evidence.

2. The subject property is a residence, a guesthouse and other improvements located on a 13.48-acre parcel on Shelter Island, Flathead Lake, with the following legal description:

   > Tract 1, Certificate of Survey No. 4776, Section 28, Township 25N, Range 20W, County of Lake, State of Montana, Geocode 15-3583-28-4-01-01-0000. Ex. 10 ABBEY-DOR 00018.

3. The DOR appraised Abbey's land and improvements based on the cost approach method. Ex. 44 ABBEY-DOR 001780. The cost approach finds market value by accounting for the actual cost of construction of improvements less any depreciation and obsolescence. The cost approach's widest application is in the appraisal of properties where the lack of adequate market and income data precludes the reasonable application of other traditional market approaches [such as the sales comparison approach and the income approach.] Montana Appraisal Manual at 15.

4. The DOR provided the Montana Property Record Card from its Computer Assisted Mass Appraisal (CAMA) system for the subject property. Ex. 13 ABBEY-DOR 000037-000040.

5. DOR appraiser, Don Leuty conducted the DOR appraisal of the subject property. He had been an insurance adjuster appraising houses, boats, and improvements for nearly 20 years prior to being hired as an appraiser for the DOR. Tr. 553:8-554:18. Before his retirement in 2013[1], Leuty worked for the DOR as an appraiser for nearly 14 years. Tr. 557:14-21. Leuty testified that he had taken some real estate appraisal classes during the 1990s, and more recently completed the International Association of Appraising Officers (IAAO) appraisal classes through the DOR. Tr. 553: 8-14. Leuty testified that he has appraised commercial, residential and agricultural properties in the Kalispell, Whitefish and the Flathead Lake areas as part of his job as an appraiser for DOR. Tr. 558: 1-7.

6. Leuty testified he appraised 20 single-family homes worth over $5 million and a few homes valued in excess of $10 million. Tr. 562:19-20 - 563:5-9.

7. Leuty testified that the cost approach is a common method used to value high-cost homes, when there are few or no comparable sales. Tr. 563:15-564:4-6.

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[1] Leuty had been retired for seven months in November 2014. Tr. 552:19.

8. DOR provided the appraisal work file, a real estate listing of the subject property for $78.8 million[2], and photographs of the subject property. Ex. 19 ABBEY-DOR 000252-000253; Ex. 20 ABBEY-DOR 000255-000273.

9. DOR determined that the improvements were subject to a two percent reduction in value for obsolescence/physical depreciation. Tr. 584:4-8. Williams testified that the two percent depreciation was determined using trend tables developed by DOR using cost values of every property in Montana. Tr. 708:4-709:7.

10. Leuty determined that because the improvements were virtually brand-new they did not need to be depreciated by more than two percent for physical depreciation. Tr. 584:3-10.

11. Williams testified that the application of two percent depreciation yielded a discount of over $800,000 in value. Tr. 709:14.

12. The DOR's 2014 property record card for Shelter Island shows that the DOR only applied a one percent depreciation reduction to the main house. Ex. 13 ABBEY-DOR 000039.

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[2] The testimony and other documentary evidence established that the property was listed at $105 million (Ex. 38 ABBEY-DOR 000979; Ex. 1 ABBEY-DOR at 14) before being reduced to $78.8 million. Other testimony indicated that the subject property was also listed at $59.5 million. Tr. 307:11; Ex. 1 ABBEY-DOR at 14.

13. For tax year 2012, the DOR appraised the subject property at a total value of $55,343,220. Ex. 10 ABBEY-DOR 000019. The land was valued at $3,715,785. The improvements upon the land were valued at $51,627,435. *Id.* at 000024; *see also* CTAB Appeal Form.

14. The Taxpayer filed an AB-26 request for informal review form with the DOR on October 17, 2012. Ex. 10 ABBEY-DOR 000018.

15. During the informal review, DOR reduced the subject improvement value because Taxpayer, through its attorney, demonstrated to the satisfaction of the DOR that Taxpayer was entitled to a $9,785,180 deduction for cost overruns, including various construction and engineering mistakes that had substantially increased building costs. DOR Leuty Letter, January 30, 2013, Ex.10 ABBEY-DOR 000019. Leuty concluded, "I feel that there is no question that fraud, larceny and various construction and engineering mistakes had a fairly substantial impact on building costs." Id. DOR found it "fair and reasonable to adjust the cost derived market value accordingly." Id. The DOR appraiser took Taxpayer's attorney, Mr. John Mercer, at his word and granted the full amount of reductions requested based on the estimates of these costs Mercer provided. Tr. 741:6-14. There is no evidence in the record that DOR verified the accuracy or reliability of the information used to grant the discount.

16. After applying the $9,785,180 reduction for cost overruns, the DOR determined the Replacement Cost New Less Depreciation as $31,679,850 and added a residential flat value of $9.5 million for "miscellaneous services and support structures" such as the generator buildings, the boat-capturing system, several docking systems with automated boat retrieval systems, and the underground shooting range. Ex. 45 ABBEY-DOR 001784; Ex.13 ABBEY-DOR 000037-000040.

17. At the conclusion of the informal review process, DOR reduced the subject improvements' cost-derived market value to $41,842,255, (AB 26 response dated January 30, 2013.) DOR finalized the total value of the land and the improvements after DOR's informal review at $45,558,040. Ex.10 ABBEY-DOR 000019.

18. The Taxpayer filed an appeal with the Lake County Tax Appeal Board (CTAB) on February 25, 2013, requesting a land value of $2,133,000 and an improvement value of $10,407,000. CTAB Appeal Form.

19. The Lake CTAB heard the appeal on August 27, 2013, and affirmed the DOR's revised appraised values. CTAB Appeal Form.

20. The Taxpayer appealed to this Board on September 11, 2013, stating on its Appeal form:

    i. The [DOR] failed to meet the burden of "providing documented evidence to support its assessed values."

ii. Taxpayer contends [DOR] appraiser was not qualified.

iii. The [DOR] failed to value the property at its market value as defined by statute. (M.C.A. § 15-8-111(a)and 15-8-111 (2)a).

iv. Taxpayer contends the [DOR] should have paid for an independent fee appraisal.

v. Taxpayer contends [DOR's] CAMA system is not adequate to find value. Taxpayer claims the unique nature of the improvements excluded them from mass appraisal techniques.

vi. The [DOR], in relying on actual costs, failed to take into account the significant additional costs incurred resulting from building on an island.

vii. The [DOR] failed to adjust its cost figures for physical depreciation, functional obsolescence, and economic obsolescence. Taxpayer contends it was a fundamental failure to allow only a [two percent] adjustment for obsolescence.

viii. The [DOR] failed to adjust its replacement cost analysis for "equal utility" as required by its own Appraisal Manual.

ix. In valuing the property, the DOR failed to adjust the value to reflect the high cost of owning and operating the property.

x. The [DOR] failed to equalize the value of the subject property with other similarly situated properties. Comparable properties used for valuation must represent

similar properties within an acceptable proximity of the property being valued. Mont. Code Ann. § 15-8-111(3).

xi. Contrary to established principles of construction law [sic], (the Board presumes Taxpayer intended "constitutional law"), the [DOR] singled out this Taxpayer for discriminatory or selective enforcement of the tax law. The Montana Constitution provides that, "No person shall be denied the equal protection of the laws." Mont. Const. art. II, § 4. "[T]axing authorities may not single out one Taxpayer for discriminatory, or selective, enforcement of a tax law that should apply equally to all similarly situated Taxpayers." *Penn Phillips Lands, Inc., v. State Tax Commn.*, 430 P.2d 345, 352 (Or. 1976).

xii. The [DOR] misapplied the cost approach to valuation by failing to develop a value for the property other than consideration of the actual costs of the project.

xiii. The [DOR] applied a capitalization of income method from a hypothetical source with no "back-up" data, and failed to justify its use.

xiv. The [DOR] presented inaccurate information through the form of a marketing video, which contains information, which is not only inaccurate but also irrelevant to a proper determination of value.

xv. The [DOR] "relied upon" listing prices found on the internet.

xvi. The [DOR's] appraiser misapplied the concept of entrepreneurial profit in his valuation analysis and failed to

apply functional obsolescence and the factors commonly associated therewith.

xvii. The [DOR's] appraiser failed to extract market reactions from sales of higher priced properties in relation to their Reproduction Cost New (RCN). This method should be used as a measure of both functional and economic obsolescence.

xviii. The [DOR's] appraiser and the appraisal prepared did not conform to the USPAP standards for mass appraisal of property for tax purposes. (Appeal Form attachment, Ex. A.)

21. DOR avers as follows (as set out in the final pre-trial order):

i. The Board, a quasi-judicial body, may not determine issues of constitutional law.

ii. The DOR's assessment of Abbey's improvements is based on accepted valuation methodologies and is reflective of the property's fair market value as of [the lien date].

iii. DOR [used] CAMA [to] determine a value for the Abbey property because Montana is a mass appraisal state.

iv. Abbey's experts did not prove that the CAMA system was incapable of valuing unique properties.

v. Section 15-8-111(3), MCA permits DOR to use information available from any source in determining market value, including comparable properties outside the Flathead Valley and outside Montana.

vi. During the AB26 Informal Review, the actual costs verified that the DOR's appraisal using CAMA was within an acceptable range of values.

vii. During the informal appeal process, DOR subtracted $9,785,180.00 because Abbey/Land LLC, through its attorney, provided documentation of cost overruns, fraud, engineering mistakes, and other costs.

viii. The cost approach as employed by DOR fully accounts for all forms of depreciation and/or obsolescence. In addition, DOR determined the Abbey[/Land LLC] improvements were subject to a two [percent] reduction in value for physical depreciation.

ix. Abbey's contention that a trophy or novelty home built to the exact specifications of a single person has no value in the market has no basis in Montana law or appraisal practice.

x. DOR's assessments [are] entitled to a presumption of correctness provided the assessment is in accordance with Montana statutes, administrative rules and regulations, and those statutes, rules, and regulations are not arbitrary and capricious, or otherwise unlawful.

xi. Abbey/Land LLC has not overcome the presumption of correctness afforded the DOR's assessment by showing by a preponderance of the evidence that the assessment does not reflect the market value of the property.

xii. Scores and ratings provided by [Taxpayer's] expert witness ranking Montana against other states for taxation purposes have no bearing on the market value of the subject property.

xiii. Taxpayer has not met the burden to prevail, to wit, the Taxpayer has not proved (1) that there are several other properties within a reasonable area similar and comparable to his; (2) the amount of assessment on these properties; (3) the actual value of the comparable properties; (4) the actual value of his property; (5) the assessment complained of; (6) that by comparison his property is assessed at a higher proportion of its actual value that the ratio existing between the assessed and actual valuations of similar and comparable properties, thus creating discrimination *DeVoe v. Dep't of Revenue of Montana*, 233 Mont. 190, 759 P.2d 991 (1988).

xiv. Stevens' appraisal is drastically under-valued and inadequate because it does not comply with the Uniform Standards of Professional Appraisal Practice (USPAP), among other flaws.

xv. Montana Law, as well as the *Montana Appraisal Manual,* allows DOR to assess fair market value of a property according to the cost approach and allowing either replacement cost or reproduction cost depending on the circumstances of the appraisal.

xvi. The Board should disregard the general reports or testimony related to costs of construction generally, market analyses, obsolescence from an architectural standpoint, the treatment of "high-net worth individuals," or the "tax load" estimated by fee appraisers. These have no bearing on the actual fair market value of the subject property. *See Final Pre-Trial Order, October 20, 2014.*

22. On September 5, 2012, Leuty travelled to the subject property for a new construction review or onsite inspection. Leuty took measurements, verified the dimensions of the subject improvements, and took photographs. Ex. 13 ABBEY-DOR 000037; Tr. 569: 14-24.

23. During the site inspection, Leuty verbally requested the actual costs of construction information from the Taxpayer's representative. On October 22, 2012, Leuty formally requested the actual cost information by sending a letter to John Mercer, the Taxpayer's attorney. *See* Ex. 12 ABBEY-DOR 000033, Tr. 572:2-9.

24. Leuty testified that he determined there were no sales of comparable properties anywhere else in the world, including other prime Montana real estate markets beyond the Flathead Lake area, such as in the Yellowstone Club near Bozeman, or Whitefish. As a result, DOR opted for the cost approach as the most defensible methodology for valuing such a unique property instead of the market approach. Tr. 669:5-16, 670:10-16.

25. After the site inspection, DOR endeavored to quantify costs of construction for the subject property. Leuty testified that because of the nature of the opulence of the "trophy property" it became "self-evident" that DOR cost tables used to estimate value were going to be "totally inaccurate." Tr. 573:18-574:8. Adjustments were going to

have to be made for architecture, quality of materials, design, artisanship, and construction of the property. Id.

26. With the help of Leuty's supervisor, Mr. Scott Williams, a general IAAO-certified appraiser and current DOR regional manager, Leuty performed the cost-based CAMA appraisal based on the inputs from the property inspection of Shelter Island. Tr. 576:15-20.

27. Leuty applied the highest grade available under the CAMA system to value the subject improvements. Leuty applied a Grade Factor 10+ (Extraordinary)[3], a cost a design Factor of 1.75[4], and an Economic Condition Factor (ECF) of 1.75[5] to adjust the value of the Replacement Cost New upwards. See Ex. 13 ABBEY-DOR 000039.

28. The upward adjustments were applied based on the appraiser's judgment that the subject property used the best quality of materials, high-end finishes, high quality of workmanship, and excellent architectural detail. See Tr. 561: 6-8.

29. Williams testified that the ECF number was not calculated in the traditional manner by county, rather, in this instance the DOR performed a manual calculation to "allow, encourage, nudge" the

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[3] This factor raises the value of the subject property 5.85 times that of an ordinary home.
[4] This factor raises the value of the subject property by 175 percent.
[5] This factor raises the value of the subject property by an additional 175 percent.

CAMA system to generate a cost-based valuation that the DOR determined was closer to the actual market value. Tr. 751:1-7.

30. Leuty testified that there were "enhancements, additions and atypical functions" associated with the subject property that the CAMA system was not designed to capture, "no matter what [he] did." Tr. 580:5-13.

31. For these enhancements, "miscellaneous services, and support structures" such as the heated limestone terrace, the generator buildings, the boat-capturing system, several docking systems with automated boat retrieval systems, and the underground shooting range, Leuty added $9.5 million under the "miscellaneous services and support structure cost." Much of the testimony given at the hearing approximates this figure to $10 million. Tr. 580:5-25. *See also* Ex. 45 ABBEY-DOR 001784. The record does not provide a clear account for how Mr. Leuty arrived at this flat value.

32. DOR used the internet to research and look worldwide for prospective comparable properties. Tr. 574:3-576:11. DOR used these listings as a starting point in determining a range of values that would be appropriate for the kinds of high-end improvements in the subject property. Tr. 643:4-18.

33. From his research, the DOR appraiser estimated the range of $1,500 to $2,000 per square foot as a "benchmark" by which to gauge the CAMA system appraisal for the improvements. Tr. 590:16-17.

34. Williams testified that the internet research was used to create a base line from which to assess the reasonableness of the appraisal per-square-foot value range for the subject improvements. Leuty also testified that he used different luxury properties from the internet to "extrapolate" to what would be a reasonable per-square-foot cost of construction, given the quality of materials and the extraordinary amenities found in the subject property. Tr. 575:1- 576:23.

35. Williams cited Section 15-8-111(3), MCA for the proposition that Montana law allows the DOR to conduct research from any source, as long as it is deemed reliable. Tr. 702:2-17. He testified, "[i]t's not unusual to go on the internet ... and...start researching." Id.

36. Williams testified that the Two Bear property in Whitefish, Montana was a similar property for valuation purposes and this property was valued at $38 million. See Tr. 726:1-14.

37. When Mr. Leuty was preparing the initial appraisal, Taxpayer had not provided actual cost information to inform his appraisal. Tr. 574:9-15.

38. Williams testified that during the informal review process, Taxpayer provided a spreadsheet listing its cost overruns. Tr. 693:17-23.

39. Based on Taxpayer's cost overruns as provided, Williams was "comfortable" granting a reduction and he authorized the $9.8 million discount to account for various cost overruns and other expenses that did not directly contribute to value. Tr. 693:1-25, 694-1.

40. On November 8, 2012, DOR received an additional spreadsheet of actual costs expended on the property. Ex. 31 ABBEY-DOR 000581. Taxpayer submitted an overall cost compilation summary showing that the actual job costs totaled $37,266,973.08. Ex. 32 ABBEY-DOR 000582. However, other costs from the compilation totaled an additional $19,746,809. *Id.* The Job cost worksheet is dated June 6, 2012. *Id.*

41. Prior to 2012, DOR assessed a flat value, which reflected that the improvements were 50 percent complete. Tr. 569:1 -13. The property was completed in 2012 (the tax year at issue), and the property was considered fully complete for tax purposes in that year. Tr. 697:13-16.

42. Taxpayer hired Mr. Thomas Stevens of Missoula, Montana to conduct an independent appraisal and to report on an estimate of value. Stevens has many years of experience as an appraiser and has both MAI and SRA designations from the Appraisal Institute. *See* Ex. 1 A/L0051 – A/L 000197.

43. Stevens prepared two appraisal reports. The first report dated August 15, 2013, was submitted for the CTAB hearing (Stevens I). Ex. 28 ABBEY-DOR 000417-000461. The second report dated February 2, 2014, was submitted for the appeal to this Board (Stevens II). Ex. 1 A/L 00051-A/L 00097.

44. Stevens I valued the subject property using the replacement cost methodology. See Ex. 28; Tr. 89:7-12. Stevens I considered other exclusive and costly Montana residential properties and made a comparison of them to the subject. This report estimated the subject improvements to be worth $9.8 million as of the July 1, 2008 lien date. Tr. 88:8-10.

45. Stevens II includes a discussion of the ratio of tax load to the assessed value and an equalization analysis. Ex. 1. Stevens II concluded that the subject property is "grossly overvalued." *Id.*

46. Stevens testified that he closely observed the northwest Montana real estate market for lakefront homes around Flathead Lake, and prices were appreciating at the rate of 15-25 percent per year until January 2007. Tr. 67:23 – 68:5.

47. According to Stevens, the economic downturn severely and adversely affected real estate market in Montana. Tr. 64:4-70:15.

48. According to Stevens, there was an eighteen-month period after 2007 when not a single waterfront property on Flathead Lake area sold. Tr. 108:3-16.

49. Stevens testified that the calculations within his report recognized and appropriately discounted for economic obsolescence, functional obsolescence, and super adequacy associated with the subject property as compared to other high-valued residential properties in Montana. Tr. 92-93.

50. Stevens testified that he did not consider properties outside of Montana because he did not think he could calculate an accurate location adjustment for comparable properties not in Montana. Tr. 102:17-103:4

51. Upon realizing that his cost approach appraisal was significantly below Mr. Abbey's construction costs, Stevens consulted with an appraiser in Bozeman, Mr. Keith O'Reilly. Tr. 93:12-25.

52. Stevens testified that O'Reilly has appraised most of the high-value homes in the Yellowstone Club Development near Big Sky, Montana. Tr. 93:13-25.

53. Stevens testified that O'Reilly provided cost estimates for the highest, most exclusive residential development in the Yellowstone Club as valued in the range of $750-950 per square foot. Id.

54. Based on that estimate, Stevens used both the low and high ranges to calculate a replacement cost for the subject property. Tr. 94: 11:17

55. Stevens then computed an average replacement cost after adding an additional construction cost of 25 percent to account for the island location (the difficulty of transporting personnel and materials to the island.) *Id.* The replacement cost computed came up to about $14 million prior to deductions for any depreciation or obsolescence. *Id.*

56. Stevens determined that in addition to an island premium of 25 percent, and a premium for contractor's overhead and profit of 15 percent, the subject property suffered from incurable super adequacies and external obsolescence that needed to be subtracted from the replacement cost. Tr.95:6-21; Ex. 1 A/L 00074.

57. Based on his experience and judgment, Stevens settled on an obsolescence discount of 30 percent. Tr. 97:6-7.

58. After deducting the functional obsolescence, the Stevens II concluded that the final value for the subject property was $9,800,000. Tr. 97:16.

59. DOR's expert witnesses, Mr. Hagar and Mr. Albertini, both testified that Stevens II report was not USPAP compliant and did not make the scope of work clear in the report. See Ex. 46; Tr. 425:13-18.

60. When asked on cross-examination where Stevens derived the formula used to estimate the discounts for obsolescence and super adequacy, Stevens responded "it's simple math." Tr. 177:12.

61. On cross-examination, Stevens acknowledged a fundamental math error in his analysis of the Stone Crop Property, a comparable property used in his final calculation. The error led to a discount of 70 percent. DOR contended that the correct value using Stevens' formula should have been only 41 percent for that comparable. Tr. 196:4-17.

62. On cross-examination, Stevens was unable to explain why he chose specific values for functional obsolescence and his basis for applying blanket cost additions in value his comparable properties. *Id.*

63. Taxpayer's expert witness Joe Crosby from Cumberland, Maine, testified that he was a public policy expert with a background in state taxation policy. Crosby works as a Legislative Director for the Council on State Taxation (COST) in Washington D.C., which publishes various national ratings and comparisons of state taxation in the United States. Tr. 44:4-12.

64. Crosby testified that non-residential vacation homes have been over assessed not just in Montana but nationwide, and that property tax provisions historically gave preferential treatment to full-time property

owners that is not provided to nonresidents or to those who have vacation homes. Tr. 44:13-24.

65. Crosby testified that he was not qualified to make any judgment of market value on the subject property and had not done so. Tr. 30:18-25.

66. Dr. John R. Smith, Montana State University Bozeman Professor of Architecture, who has taught, lectured and practiced architecture in the western United States, testified on "super adequacy." Tr. 255-266.

67. Dr. Smith specializes in the intersection of eastern and western philosophy as it relates to architecture. Tr. 235:12-14.

68. According to Dr. Smith's opinion, the subject property's architectural style was "eclectic and false and inappropriate." Tr. 265:8-11. As a result, the unique style would reduce the desirability to potential buyers and thus reduce the value of the subject property. Tr. 266:5-8.

69. Dr. Smith testified that high-end clients would all want "their own dream." Therefore, the Taxpayer would have a very difficult or impossible time finding a buyer who, if they could afford the subject property, would not prefer to build their own different "dream" rather than purchasing the vision expressed by Donald Abbey in his residence. Tr. 266:1-4.

70. Dr. Smith considered the subject property to be a "replica building" and essentially a modern-day castle, Tr. 259:24-260:6; thus, it would appeal to very few high-end clients who all would want their own dream. Tr. 266:1-4.

71. Lake County Realtor Mr. Mac Swan, an experienced Realtor/Broker from Polson Montana, testified in support of the November 19, 2012 market analysis Swan performed with Rod Stell estimating the value of the subject property at $12.54 million. Tr. 304:8-11. Swan testified he had been involved with three sales of over one million dollars during his career as a realtor in the Flathead Lake region. Tr. 288-289. Swan describes the property as "extraordinary," Tr. 311:20 and "way out of the norm." Tr. 329:14. Swan also opined that the "super-adequacy" of the materials used in construction would hamper the marketability of the subject property. Tr. 303:12-15.

72. Swan opined that the total market value of the subject property was somewhere between $12 million and $13 million as of the 2008 lien date. Tr. 296:6-11. His report valued the improvements at $10,221,000. Tr. 317:9-11. Swan supported his valuation by the fact that actual sales values of property in the Flathead Valley were 46 to 55 percent below the sales during the 2007 pre-recession, "boom days." Tr. 284:11-25.

73. The owner of the subject property, Donald Abbey, testified as the designer and the general contractor of the subject property. Tr. 336:2.

74. He estimated that he had incurred costs in excess of $35 million to develop and construct the property. Tr. 339:5-10. See also Ex. 32 ABBEY-DOR 000582.

75. He testified that the property was currently for sale, listed with a broker who had significant experience marketing high value properties around the globe. Tr. 342:4-14.

76. Abbey estimated that the property would eventually sell for a price in the neighborhood of $10 million. Tr. 342:14.

77. Taxpayer called Greg Thornquist, a general certified appraiser and a former Montana Tax Appeal Board chair, as a rebuttal witness. Tr. 759:21-24. Taxpayer hired Thornquist to review Stevens Reports for compliance with USPAP (Tr. 768:3-15), and to rebut the Hagar-Albertini report and testimonies. Tr. 776:4-25; Tr. 777:1-19.

Principles of Law

1. The Montana Tax Appeal Board has jurisdiction over this matter. (§15-2-301, MCA.)
2. All taxable property must be assessed at 100 percent of its market value except as otherwise provided. (§15-8-111, MCA.)
3. Market value is the value at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts. (§15-8-111(2)(a), MCA.)
4. The appraised value supported by the most defensible valuation information serves as the value for ad valorem tax purposes. ARM 42.18.110(12); *Rainbow Senior Living of Great Falls v. Montana Department of Revenue*, 2013 WL 6062167; *Keck v. Montana Department of Revenue*, 2013 WL 2476838.
5. For the taxable years from January 1, 2009, through December 31, 2014, all class four properties must be appraised at market value as of July 1, 2008. ARM 42.18.124(b); *Rainbow Senior Living of Great Falls v. Montana Department of Revenue*, 2013 WL 6062167; *Keck v. Department of Revenue*, 2013 WL 2476838.

6. The Montana Tax Appeal Board must give an administrative rule full effect unless the board finds a rule arbitrary, capricious, or otherwise unlawful. §15-2-301(4), MCA.

Findings of Fact, Conclusions of Law and Board Discussion

The Board must determine, based on a preponderance of the evidence, whether the DOR set an appropriate value on the subject improvements for tax year 2012.

The Board has authority to hear evidence, find the facts, apply the law, and arrive at a proper value for the subject property. Generally, the assessed value of the Department of Revenue is presumed to be correct and the Taxpayer must overcome this presumption. The Department of Revenue however, bears a certain burden of providing documented evidence to support its assessed values. *Farmers Union Cent. Exch. v. Department of Revenue*, 272 Mont. 471, 901 P.2d 561, 564 (1995); *Western Airlines, Inc. v. Michunovich*, 149 Mont. 347, 353, 428 P. 2d 3, 7, cert. denied 389 U.S. 952, 19 L. Ed. 2d 363, 88 S. Ct. 336 (1967.)

We note that the instant case is about the most credible method for determining the market value for a unique high-end property on an island in Flathead Lake based on the evidence presented to this Board. While the DOR struggled using its typical methods to value the subject property because the

subject may be one of the most lavish residences ever built in Montana, we find that the Taxpayer failed to provide enough credible evidence to dislodge the DOR's valuation. The Taxpayer did not meet its burden of proof to overcome the value assigned by DOR. Ultimately, we find that the DOR's evidence was the most credible in setting a market value for the subject property.

An appraisal is an opinion or estimate of value. Montana Appraisal Manual at 13. It is the appraiser's responsibility to determine, through the appraisal process, the full market value of the property as of the appraisal date. Id. This process is not necessarily a purely scientific process. The DOR appraiser applies the CAMA system, his/her experience, education, and training, considers supporting market data from various sources, along with their best judgment to determine an opinion or estimate of value.

As noted in *Pacificorp v. DOR* (CT-2005-3; July 2007), the DOR is tasked with mass appraisal valuation which requires a small number of DOR employees to assess a large number of statewide properties using standardized appraisal techniques and procedures to achieve a uniform equitable valuation in a compressed time period with limited information. *See also* Montana Appraisal Manual at 468. While these factors do not relieve the DOR of its obligation to conduct accurate, professional appraisals, those factors do make it necessary for the DOR to use mass appraisal methods to enable the DOR to complete its

assigned task within a timeframe determined by the Montana Legislature within a budget authorized by the Montana Legislature.

With limited resources juxtaposed against a backdrop of nearly one million properties to assess in Montana, there is an appropriate role for mass appraisal of residential properties. This notion has been upheld in many cases by higher Montana courts through the years since statewide valuation was assigned to the DOR in the 1970's. Moreover, Montana law does not require the DOR to hire independent outside appraisers to value individual properties.

The role of this Board is to provide an independent review of individual properties appraised by the DOR's mass appraisal system. This role becomes more significant for atypical residences such as the subject property. The subject improvements were built to a much higher standard than a typical Montana home. The DOR's existing mass appraisal software system capabilities are designed with a more typical Montana residential property in mind.

The Montana Supreme Court has allowed the DOR to use any of the three accepted approaches to appraise a property, market, income, and/or the cost approach, depending on available data. *Albright v. State By & Through State*, 281 Mont. 196, 201, 933 P.2d 815, 818 (1997). Given the statutory definition of market value, that is, the value at which property would change hands

between a willing buyer and a willing seller, the "market" approach using comparable sales is the preferred approach in valuing residential property when adequate data is available. The cost approach is used to value residential property when comparable sales data is unavailable due to the uniqueness of the subject property or a lack of sales of comparable properties in the area. Id.; See Montana Appraisal Manual, at 15. Construction costs alone, however, are insufficient to determine a cost-based valuation, without considering other relevant market data. See e.g. *DeVoe*, 866 P.2d at 235; *Albright*, 933 P.2d at 822.

DOR's Cost Approach

The DOR valued the subject improvements, a newly built high-end home on an island in Flathead Lake, using the cost approach. Tr. 569:1 -13; Ex. 45 ABBEY-DOR 001784. The cost approach consists of estimating either the replacement or the reproduction costs of improvements and deducting therefrom any loss in value because of physical deterioration and/or functional obsolescence. Montana Appraisal Manual at 15; § 15-8-111(2)(b), MCA. The cost approach is based on the proposition that an informed purchaser will not pay any more than the cost of producing a substitute property with the same utility as the subject property. Montana Appraisal Manual at 14. According to the Montana Appraisal Manual used by the DOR, "The informed buyer is not justified in paying anything more for a property than what it would cost him to

acquire an equally desirable substitute property. Likewise, the upper limit of value of most improvements is the cost of reproducing an equally desirable substitute improvement." See Ex. 41.3 ABBEY-DOR 001552.

We agree that the DOR's decision to use the cost method to appraise the subject property was the most reliable appraisal method to determine the true market value for this unique property. Everyone who testified at the hearing agreed that finding appropriate comparable sales to conduct a reliable market appraisal for the subject property was a very difficult task. Market methodology can at best provide credible supporting information to back up a value determined through cost methodology. We agree with both parties that the income method should not be considered to value the subject property.

We also find that the DOR's actual methodology to determine a value for the subject property (to be described more fully in the pages that follow) was sufficient to meet its burden to provide evidence in support of its value. The testimony established the rationale behind the DOR's determination. The DOR appraisers had personal knowledge that actual costs of construction for high-end homes in both the Whitefish area and the Yellowstone Club range from $650-$1,000 per square-foot. Given the extraordinary materials, extraordinary architectural detail, extraordinary craftsmanship, and the additional expenses associated with building on an island, this Board finds it

reasonable to conclude that the DOR appraisers correctly determined that the cost of building Shelter Island exceeded $1,000 per square foot.

The subject improvements were under construction for over ten years. During this time the DOR valued the property at a flat value and as 50 percent complete. Tr.569:8-10. In 2012, Williams saw that the property was listed for sale and determined that the DOR needed to conduct an appraisal of the completed improvements for property tax purposes. Tr. 568:16-24. Williams assigned the appraisal task to Leuty, but remained very involved throughout and frequently consulted with Leuty during the process. See Evidence Presented ¶ 26.

On September 5, 2014, Leuty conducted a "new construction review" or a site inspection of the property. Tr.569:19-24; *see also* Ex. 13 DOR-ABBEY 000037. Taxpayer's attorney Mercer and the property's caretaker accompanied Leuty during the site inspection. Tr.571:13-17. Leuty was provided with unrestricted access to measure the dimensions of the improvements, take photographs, and view all of the property's rooms, mechanical systems, and finishes. Leuty testified that the home had extraordinary features, many that he had never seen in any of the higher-end properties that he has appraised over his career. Tr.571:1-3. For example, the windows in the bathroom transform into a television or a mirror at the touch of a button. Tr.571:4-6. However,

Leuty recognized that the more problematic improvements for his valuation purposes were the customized features, including a mechanized rail system that can bring boats and their occupants directly into the main house or boathouse from docks located on the island, an underground shooting range, a 10,000 square-foot heated limestone terrace, and sea walls constructed along the lakeshore. Tr. 580:5-13. During the site visit, Leuty asked Mercer to provide him with Taxpayer's actual cost of construction information to help him estimate a market value that would reflect the the materials used and the quality of craftsmanship. Tr. 572-573: 22-25 1-4.

After the site inspection, Leuty reviewed the photographs with Williams and discussed how best to proceed with the appraisal. It was self-evident to Leuty that the DOR's Computer Assisted Mass Appraisal (CAMA) System, which uses standardized construction cost tables to determine cost estimates, was not going to be able to determine an accurate cost value for the subject property without further adjustments to reflect the high quality of the improvements. Tr.573:18-25. Leuty, at Williams' direction, utilized the internet to find similar homes in order to derive a reasonable per-square-foot estimate to use as a baseline for comparison to the subject property's construction cost. Tr.574:3-8. Using information derived in part from that

research, Leuty concluded that a reasonable range of construction cost for the subject property would be $1,500 to $2,000 per square foot. Tr. 575:20-21.

Williams testified that he had cultivated professional relationships with the area contractors and appraisers in order to obtain accurate construction costs for some of the multi-million dollar homes built in the Iron Horse subdivision. Tr.714:6-25 715:1-13. As an example, Williams knew that a particular home used in the Stevens Report located at 113 Huckleberry Lane cost $500 per square foot to build but was of inferior quality to the subject property.[6] Tr. 714:17. Williams also consulted with DOR appraisers who work in DOR's Madison County office. These appraisers value the multi-million dollar homes built in the Yellowstone Club. Tr. 700:22-25; Tr. 701:1-13. Williams gave one example of a home in the Yellowstone Club that appraised for $17,000,000. This particular home is 10,000 square feet smaller, and of inferior quality, than the subject property. Tr. 701:1-13. This home was appraised at $1,000 per square foot, which was consistent with other high-end trophy homes typically built in Montana. Tr. 701:1-17. Given the extraordinary and superior architecture and quality of the subject property, along with the additional costs of building on an island, Williams concluded

[6] This testimony was meant to suggest that Stevens cherry picked under-valued comparables and therefore his $340.28 base cost-per-square foot computation of the subject property was under-valued. See Section on Abbey/Land LLC Appraisals.

that Leuty's cost estimate range of $1,500 to $2,000 per square foot appeared reasonable based on his professional experience and personal knowledge of the cost of construction of other high-end homes.

Contrary to Crosby's opinion on the issue, the DOR did not rely on an internet search to arrive at a per square foot value to conduct their appraisal. Williams Dep. 32:16 – 35:15. The record indicates that the DOR used the internet to research broadly the cost of constructing an equivalent trophy home. The DOR's appraisers used their professional experience and personal knowledge of the costs of construction of other high-end homes built in Montana and compared this range against known cost information of homes to gain confidence that their estimate was reasonable. Tr. 727:23-25 728:1-2.

Cognizant of this range, Williams supervised Leuty's appraisal of the subject property using the CAMA system. Leuty entered all of the requisite site data measurements into the CAMA system to determine the square footage and some of the property's unique features that could be accounted for in the CAMA system. Part of the CAMA analysis requires the appraiser to enter a grade for the quality of the improvements. According the Montana Appraisal Manual a grade 5 is an average quality residence. Montana Appraisal Manual at 267. Extraordinary residences are given a grade 10, the highest grade available in the CAMA system. Montana Appraisal Manual at 277. The grade affects

the appraised value of the property as follows: the CAMA system uses the cost tables to calculate a per square foot value for any given property. The tables are created for the cost of constructing an average home, so a home with a grade 5 would be appraised at 100 percent of the value determined by CAMA system. Increasing the grade factor increases the appraised value by simply multiplying the 'grade 5 average value' by a percentage to reflect the fact that the home under appraisal is of higher quality than an average house. A grade 10+ (Extraordinary) increases the appraised value by 585 percent to reflect the cost of building a higher grade home.

Both Leuty and Williams reasonably believed that the cost per-square-foot as determined by the CAMA system for a grade 10+ residence would significantly underestimate the true full market value of the subject property, given their knowledge of the architecture, quality, design, and construction of the improvements. As testified to by all the witnesses, the finest materials and craftsmanship were used in the construction of these improvements. For example, every room has custom-made light fixtures; the living room is paneled with African mahogany; the roof was constructed of blue Virginia slate with custom copper trim (as opposed to the conventional asphalt or wood shingles); the walls are two-feet-thick blocks of stone (not the regular 2-by-6 wood frame), imported Vietnamese marble flooring (as opposed to regular

hardwood), Italian plaster ceilings and imported limestone tiles. Tr. 90:22-92:5; Tr. 101:16-21. Given the overwhelming and uncontroverted testimony that the improvements on Shelter Island may be the most lavish of any property ever built in Montana, the DOR's appraisers reasonably concluded that the construction costs of Shelter Island exceeded the software appraisal limitations imposed by the CAMA system. Tr. 753:7-16. The appraiser further concluded that this home would cost much more to build (the subject improvements or its replacement) than an average personal residence given the high quality of materials, design, and architecture used. See generally Tr. 620 -623.

At Williams' direction, Leuty adjusted two other factors in the CAMA system; the cost and design factor and the economic condition factor (ECF). The cost and design factor can be adjusted up to 1.99 to further increase the value of a grade 10+ property to further refine and reflect the specific quality of individual extraordinary homes. The software limits the entry value for the cost and design factor to 1.99, which Williams and Leuty determined was not sufficient. The ECF is the only other factor that performs the mathematical equivalent calculation as the cost and design factor. Normally, the ECF is a factor the DOR uses to adjust property values within neighborhoods to reflect variations in the sales prices to the costs of new construction. However, for this appraisal, Leuty entered a cost and design factor of 1.75 and an ECF of

1.75 to increase the CAMA system appraised value of the improvements by another 350 percent. These increases were intended to capture the truly extraordinary quality of the construction materials and architectural design and the quality of the craftsmanship. Tr. 751:1-10.

Exhibit 44 is the Montana residential cost report laying out detailed per square foot computation of how the main house Replacement Cost New Less Depreciation was calculated by the DOR. DOR computed the replacement cost new of the first floor, second floor, and basement of the main dwelling at $ 1,074,741 and the "adjustments, Additions and other Features" added another $474,227. The Total Replacement Cost New of the main house was $1,548,968 before any upward adjustments to account for the high quality of materials, design, and workmanship.

Exhibit 42 is a spreadsheet detailing DOR's Replacement Cost New for the guesthouse. DOR computed the Replacement Cost New of its first floor, second floor, and basement floor at $180,405 and the "adjustments, additions and Other Features" at $96,013. The Total Replacement Cost New of the guesthouse was $276,418 before quality adjustments. Exhibit 45 shows the docks, the limestone terrace, and the masonry of the two garages were valued as Other Building and Yard improvements' Replacement Cost calculation of $662,402.

Effects of the Adjustments and Other Features

Main House

Replacement Cost New - Residential Dwelling and Adjustments, Additions and Other Features:	$1,548,968
Cost & Design Factor	*1.75
Grade Factor - Grade 10+	*5.85
Replacement Cost New:	$15,857,560
Less Depreciation CDU = EX and Effective year 2011 99% Good	*0.99
Replacement Cost New Less Depreciation:	$15,698,984
Local Cost Index:	*0.98
ECF:	*1.75
Adjusted Dwelling Replacement Cost New Less Depreciation	$26,923,758
Adjusted Dwelling Replacement Cost New Less Depreciation	$26,923,760 rounded

Guesthouse

Replacement Cost New - Residential Dwelling and Adjustments, Additions and Other Features:	$276,418
Cost & Design Factor	*1.75
Grade Factor - Grade 10+	*5.85
Replacement Cost New:	$2,829,829
Less Depreciation CDU = EX and Effective year 2002 = 98% Good	*0.98
Replacement Cost New Less Depreciation:	$2,773,233
Local Cost Index:	*0.98
ECF:	*1.75
Adjusted Dwelling Replacement Cost New Less Depreciation	$4,756,094
Adjusted Dwelling Replacement Cost New Less Depreciation	$4,756,090 rounded

Adjusted Dwelling Replacement Cost New Less Depreciation	$31,679,850 rounded
Residential Flat value Misc. Services & Support Structures	$9,500,000
Total OBY Replacement Cost New Less Depreciation	$662,405 rounded
Total residential Dwelling RCNLD + OBY RCNLD	**$41,842,255**

Leuty included an additional $9.5 million as a flat value to cover the costs of all of the unique features for which the CAMA system does not have cost tables to determine values. These features include the underground-mechanized rail boat retrieval system and the corresponding docks, the underground shooting range, the heated limestone terrace and the sea walls. Tr. 580:5-25.

Lastly, Leuty testified that he applied a two percent depreciation reduction to account for the fact that the home was almost brand new and thus warranted a minimal reduction for physical depreciation. Leuty and Williams testified that there was no discount applied for either functional or economic obsolescence. Leuty determined that there was no reason to discount the DOR appraised value for functional obsolescence because the home was built as a 21st century modern day castle to suit Mr. Abbey's exact specifications and desired utility. Tr.661-666. Leuty determined there was no reason to discount the DOR appraised value for economic obsolescence because the DOR had data to show that sales of homes on Flathead Lake were still profitable as of the July 1, 2008 lien date and thus the market did not show any signs of economic obsolescence. Tr. 584:18-24; Tr.711:13-25; Tr. 712:1-14. This testimony was credible and indicated that the market for high-end homes

remained strong through the lien date. Therefore, substantial discounts for economic obsolescence were not warranted in this case.

Upon completion, the full market value for the land and improvements was $55 million, $3.7 million for the land and $51.3 million for the improvements. Tr. 581:1-3. The $41.8 million figure above shows the current market value set by the DOR after the CTAB appeal.

Contrary to the testimony of Leuty and Williams, the 2014 property record card for Shelter Islands shows that DOR only applied a 1 percent depreciation discount to the main residence. Ex. 13 ABBEY-DOR 000037-000040. Given the consistent and unrefuted testimony given by the DOR appraisers that it was appropriate to apply a two percent depreciation reduction to the main house, this Board finds the DOR failed to modify the property record card accordingly to reflect the two percent discount. Applying an additional one percent discount to the main residence is appropriate in this case.

Once the appraisal was completed, Leuty notified Mercer of the determination and sent out an appraisal and assessment notice. Tr.581:25 582:1-3. Upon receiving the assessment notice, the Taxpayer filed a request for an informal (AB26) review with the DOR. During the AB26 review, Mercer provided the DOR with a summary of Abbey's actual construction costs.

Leuty testified that the actual construction costs were pretty close to the appraised value – somewhere between $55 and $65 million.[8] Tr. 583:12-19. Taxpayer also provided a voluminous spreadsheet detailing at least $9.8 million in construction cost overruns, that is, work that was redone due to design and engineering mistakes. Tr.693:17-25. Williams approved a $9.8 million downward adjustment to the appraised value to allow for these overruns. Tr. 694:1-12.

After this adjustment, the DOR reached its final appraised value of $3,715,785 million for the land and $41,841,255 for the improvements. The Board orders DOR to recalculate the value of the main residence to reflect a two percent depreciation as testified to by the DOR appraisers. Other than this minor modification, this Board finds that the DOR has met its burden to provide credible and reasonable evidence in support of its appraised value. We find that the DOR appraisers reasonably relied upon their professional judgment and collective experience to determine the market value of the subject improvements.

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[8] Adding actual job costs and other costs gives a grand total of $55,512,373. See Ex. 32

Abbey/Land LLC Appraisal Reports

Taxpayer hired its own appraiser who offered appraisal reports for the subject improvements not including land.[9] *See* Stevens reports in Evidence Presented ¶ ¶ 43 – 45 above. According to Stevens, the market value of the subject property using a Replacement Cost Estimate was $9,800,000. Evidence Presented ¶ 58 above. The Stevens reports focused on the requirements in Section 15-8-111(2)(b), MCA, that the DOR "fully consider reduction in value caused by depreciation, whether through physical depreciation, functional obsolescence or economic obsolescence." The crux of Stevens II was that DOR should have computed replacement cost as the cost of constructing improvements of "equal utility" built with ordinary materials, ordinary design, and ordinary workmanship and heavily discounted for obsolescence. See Evidence presented ¶ ¶ 43 – 62 above.

Stevens prepared two appraisal reports. See ¶ 43 above. Both reports conclude that DOR's analysis was flawed and unreliable. The February 2, 2014 report differs in that it introduces into the record the concept of ratio of tax load to assessed value and a new "equalization analysis" section. Ex. 1,

[9] Stevens II states the purpose of the appraisal is to provide the best estimate of market value of the subject improvements. Ex. 1 at 6.

ABBEY-DOR 002088-002090. In the "equalization analysis," Taxpayer introduces into the record opinion evidence to support an equal protection claim. The section alleges that the Taxpayer is singled out for unfair treatment by comparing his tax load to the taxes levied on another property on Cromwell Island on Flathead Lake. The section concludes that the subject property is "improperly and grossly overvalued" and hence "over taxed." *Id.* at 002090.

Before discussing the propriety of including this material in an appraisal, we have to address Stevens' appraisal approach. Stevens begins his analysis by using replacement cost calculations from Marshall & Swift's cost guide for high value residences (class VI residences.) Stevens first determined the square footage of the subject property as 12,941.40 square feet. Secondly, Stevens determined an adjusted base cost per-square-foot of $340.28, arriving at an initial cost estimate of $5,050,450. To the initial cost estimates, Stevens added lump sum adjustments of $5,011,180 for the kitchen appliances, the home automation system, the fireplaces, the back-up generators, the detached garage, the boathouse, underground utilities, the elevator, the fire suppression system, landscaping, porches and decks. Stevens increased the total by $2,515,408 (which is 25 percent of the total lump sum additions) to reflect the added cost of shipping materials to a private island. Stevens then added 15 percent of the running total as "contractor's overhead and profit" in order to

reach a total rounded cost $14,500,000 before depreciation or obsolescence. Id. at 00072-00074.

Main house 12,941.40 SF x $340.28/SF =		$ 4,404,994[10]
Basement		
(Unfinished)5,617SF x $24.78/SF	$139,189	
(Finished) 4,960 SF x $102.07/SF	$506,267	
		$ 645,456
Sub-Total		$ 5,050,450
Total Lump Sum Additions		$ 5,011,180
		$10,061,630
Island Location + 25%		$ 2,515,408
		$12,577,038
Contractor's Overhead & Profit @ 15percent		$ 1,866,556
Total Cost before depreciation or obsolescence		$14,463,594
		$14,500,000 (rounded)

Stevens then tested the reliability of this calculation by consulting with O'Reilly[11] who informed Stevens that the cost of construction of high-end residences in the Yellowstone Club ranged from $750 to $950 per square foot for all improvements. See Evidence Presented ¶ 53. Stevens then calculated a Yellowstone Club cost comparable using the lower range provided by O'Reilly from the Yellowstone Club properties. Because these computations were close

[10] Computed correctly this will yield $4,403,700 (rounded)
[11] See Evidence presented ¶¶51-53.

in value, Stevens concluded that his cost approach before depreciation and obsolescence correlated with his data from Marshall & Swift and the data obtained from the Yellowstone Club. Stevens therefore set the replacement cost value before deductions for obsolescence and depreciation at $14,000,000. *Id.* 00074-00075.

12,941.40 SF x $750/SF	$ 9,706,050
Island Location + 25%	$ 2,426,513
	$12,132,562
12,941.40 SF x $950/SF =	$12,294,330
Island Location + 25%	$ 3,073,583
	$15,367,913
Average $850/SF	
12,941,40 SF x $850/SF =	$11,000,190
Island Location +25%	$ 2,750,048
	$13,740,238
	$14,000,000
	(rounded)

Stevens' Obsolescence

Functional and external obsolescence are a crucial part of Stevens II report. Stevens defines functional obsolescence as "an impairment of functional capacity or efficiency, which reflects a loss in value brought about by overcapacity, inadequacy, and changes in the art..." *Id.* at 00076. The Montana Appraisal Manual's definition of functional obsolescence is markedly different from Stevens' definition and does not mention "capacity or efficiency." The

Montana Appraisal Manual's definition of functional obsolescence is quoted in footnote 18. Stevens defines "external obsolescence" as the "impairment of desirability arising from factors external to the property." *Id.* at 00076. The Montana Appraisal Manual does not define "external obsolescence." Stevens II defines "incurable super adequacy" as "an item of incurable functional obsolescence cause by a super adequacy of a property component that exceeds market requirements." *Id.* at 00076.

Stevens II concludes that it had to account for these obsolescence factors in order to determine the market value of the subject property. The rationale explaining how the subject property has external obsolescence, functional obsolescence and/or incurable super adequacy is absent from Stevens II and Stevens' testimony. In addition, Stevens picked seven high value homes in Montana to measure obsolescence from known market transactions. *Id.* at 00074-00086. Stevens decided that the functional obsolescence of the properties ranged from 20 to 70 percent, with a mean of 33.71 percent. *Id.* at 00074. In his opinion, the overall depreciation for both functional and economic obsolescence was 30 percent. Stevens did not adequately explain how he deduced a 30 percent reduction. Applying the 30 percent reduction to his calculation for the cost of the subject improvements of $14,000,000 resulted in a depreciated cost of $9,800,000. *Id.* at 00086. This

sum, when divided by the square footage, results in a value of $757.26 per square foot for the subject property, which also correlates with the cost estimates of the lower range of the value of high-end properties in the Yellowstone Club that were provided to Stevens by O'Reilly. *Id.* at 00086; See Evidence Presented ¶ 53. Stevens next applied his obsolescence factors to the DOR's cost analysis.

Stevens decided that due to the exorbitant replacement costs of the subject property, its design, construction characteristics, and location on an island, the market would place the obsolescence factor at the very top allowable. Ex. 1 at 00087. In Stevens I, the report pegged obsolescence factor at 65 percent, Ex. 28 at 000453, Stevens II sets the obsolescence factor at 70 percent. *Id.* at 00087. Applying the 70 percent obsolescence figure to DOR's construction cost value of the subject property, $41,842,255, results in a value for the improvements of $12,552,676. Ex. 1 at 00087. Stevens II does not document the basis for applying a 70 percent reduction to the DOR value as opposed to the 30 percent reduction he applied to the construction cost he calculated using the Marshall & Swift methodology.

Stevens had two replacement cost calculations for the improvements. First, Stevens applied a 30 percent depreciation factor to his a calculated construction cost of $14,000,000 resulting in appraised market value of the

improvements of $9, 800,000. Secondly, he applied a 70 percent obsolescence factor to an actual construction cost of $41,842,255 resulting in a market value of the improvements of $12,552,676.

Other Taxpayer Testimony

The Taxpayer's arguments to dislodge the DOR's valuation were buttressed by witnesses who provided testimony on a number of subjects, including the appropriateness of the appraisal itself and the appropriateness of the cost methodology. Taxpayer urged the Board to adopt a "more elemental approach" in this case, and to consider whether a tax load of $370,000 was "fair" Tr. 10: 11-15. The Taxpayer also offered testimony to support its theory of "super adequacy," and how this theory should be a major factor in this appraisal's calculations.

The Taxpayer, through Donald Abbey, testified that though the property was listed for sale at $59.5 million, the listing was not meant to prompt a sale but to place him on a better footing during negotiations with his creditors. See Tr.340:1-13. Abbey testified he built the subject property on an island to re-create his childhood and his life. Tr. 352:6-16.

Crosby did not testify as an appraiser, appraisal expert or someone with particularized and personal knowledge of unique or high-end properties in Montana, but as a state legislative specialist on tax policy. Tr. 23:9-13. The

thrust of his testimony was that Montana's property tax policy would discourage high net-worth individuals from relocating, visiting Montana for the purposes of recreation, or establishing businesses in Montana. Tr. 25: 5-12. His testimony was not relevant to actual values or the methodology used by DOR in its appraisal.

Dr. Smith's testimony turned toward the philosophical. He reflected on various considerations of creativity and practicality inherent in architecture. Tr.253: 12-25; Tr. 257:18-20. His testimony linked the levels of dialectic understanding and the philosophy of Plato's Republic arising out of the allegory of the cave[12]. This opinion stood for the proposition that only the architect can appreciate true value or understand ultimate reality and that the opinion of any appraiser has no value (it was a mere shadow on the wall and not ultimate reality according to Dr. Smith). Tr.263:14-23. He concluded that the appraisal opinion of Leuty had no value.[13] Tr. 264:1. His main point was to suggest that the subject property suffered from "super adequacy" and that its

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[12] In the Allegory of the Cave, Plato has Socrates describe a gathering of people who have lived chained to the wall of a cave all of their lives, facing a blank wall. The people watch shadows projected on the wall by things passing in front of a fire behind them, and begin to designate names to these shadows. The shadows are as close as the prisoners get to viewing reality. He then explains how the philosopher is like a prisoner who is freed from the cave and comes to understand that the shadows on the wall do not make up reality at all, as he can perceive the true form of reality rather than the mere shadows seen by the prisoners. See The Allegory of The Cave Republic,VII 514 a, 2 to 517 a, 7.

[13] Like a shadow on a wall.

architectural style was "eclectic...false and inappropriate." Tr. 265: l-8. Therefore, the subject property would not be desirable to potential buyers. He did not testify as an expert in appraisal methodology. Tr. 242: 3-12.

Swan testified before the Board as an experienced Realtor/Broker in the Flathead. He described the subject property as "extraordinary," Tr. 311: 20, and "way out of the norm." Tr. 329:14. He believed that the Taxpayer's choice of construction materials was "over the top." Tr. 311:7-9. He also believed that the "super adequacy" of the materials used in construction would negatively affect market value, stating that there are some things that people (potential buyers) will not pay for. Tr. 303:12-15. Swan's market analysis placed the total value of the subject property between $12 and $13 million dollars, Tr. 296: 6-11, as of July 1, 2008, Tr. 299:5-8, with the value of the improvements at $10,221,000. Tr. 317: 9-10.

Discussion of the Taxpayer's case

The Taxpayer's case hinges on the defensibility and credibility of the Stevens reports. The Board finds that the Stevens reports do not establish by a preponderance of the evidence that their $9.8 million valuation reflects true market value as of the lien date of July 1, 2008.

The DOR presented two expert witnesses Hagar and Albertini who jointly prepared and offered a report and both gave opinion testimony. The

Hagar-Albertini report concluded that Stevens' methodology was lacking and unreliable, and that Stevens' reports were not USPAP compliant. *See* Ex.46. Thornquist[14] contradicted Hagar and Albertini through testimony supporting the USPAP compliance of Stevens' reports. Thornquist disagreed with the conclusions of the Hagar-Albertini report and found Stevens reports USPAP compliant and reliable as an appraisal of true market value based on their limited scope of work. Tr. 776: 4-25; Tr.777: 1-19. The Board had the task of sifting through the morass of data, testimony, and opinions in the record to establish the most supportable valuation.

Stevens' appraisal reports do not provide sufficient evidence to convince this Board that the market value of the subject property is $9.8 million. Though Stevens made a "personal inspection" of the subject property, Stevens' testimony did not establish that his visit was for the purpose of conducting a fee appraisal. See Ex1. at 00091. His reports do not inspire the Board's confidence in the appraised value of $9.8 million. Stevens appropriately labelled his report as an "appraisal report" as opposed to an "appraisal" per se, in order to draw a distinction that Stevens did not perform a bona fide fee appraisal. The Board does not give substantial weight to these appraisal

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[14] *see* ¶ 77, Thornquist's scope of work was to assess whether the Stevens report was USPAP compliance.

reports. These reports are inconclusive without more of the underlying formulas, work files, rationale and explanations, and are insufficient to persuade us, as triers of fact, by a preponderance of the evidence that the subject property is worth $9.8 million.

Stevens appraisal reports were unaccompanied by the full supporting work file and other documentation. The Taxpayer relied on Stevens' judgment, which is based on 38 years of experience appraising property in western Montana. Tr. 204:5-11. The Stevens II was opaque and the factual basis of any of the computations and adjustments could not be verified independently. For instance, the additions for the island location (25 percent) "contractor's overheads and profit" (15 percent), and other lump sum additions seemed random and based mostly on Stevens' judgment and experience. Credible evidence shows that Stevens picked inputs to ensure that the computation of the baseline per-square-foot cost he used in his replacement cost calculation was as low as possible. The multiplication errors, miscalculated percentages, the arbitrary rounding and rough computations also lower the credibility or the reliability of these replacement computations, making them like back-of-the-envelope calculations that we cannot rely on. Stevens' appraisal reports relied heavily on the credibility of Stevens as an expert witness and had little factual support on the record. On cross-examination, DOR highlighted some math

errors in the Stevens II report, which resulted in a huge swing in value in favor of the Taxpayer (See discussion on obsolescence.) We cannot rely on Stevens' appraised value.

We do not find the Stevens methodology credible either. Stevens defined replacement cost as "The estimated cost to construct, at current prices as of the effective appraisal date, a building with *utility equivalent* to the building being appraised, using *modern materials and current standards*, and design, and layout." Ex. 1 at 18. The central premise of Stevens' calculation of replacement cost is Stevens' assumption that a building of similar utility as the Shelter island property would be an ordinary replica constructed using ordinary materials, ordinary design, and ordinary laborers. This is a misconception of "equal utility." This Board does not accept it. Replacement cost computation must also take into account the high quality of the materials, the design, the high-end finishes, and the extraordinary amenities that the subject property currently has.

As part of the replacement cost calculation, Taxpayer identifies the Lee property as similar to the subject property. Taxpayer argues equalization requires that similar properties should be treated similarly when it comes to taxation. Equalization does not mean finding another property with wildly different characteristics, in a different state of completion, with different quality

of workmanship, as a comparable property and then citing different considerations, tax treatment or valuation methodology as indicia of unfairness. The use of the Lee property was inappropriate in large part because it was not, despite the report's suggestion, an "apples to apples" comparison. Ex. 1 at 00088-00090. This Board does not put much weight on this comparison. Given the fundamental misunderstanding of equalization, this material was not useful to the Board's determination of the accuracy of the assessed value of the subject property.

The Stevens' calculations and methodology suffer from other minor problems that diminish our confidence in its reliability. Stevens' replacement cost calculations contained errors, arbitrary values unsupported by weight of the evidence, arbitrary rounding, arbitrary premiums, and arbitrary discounts for depreciation and obsolescence. The inclusion of tax load analysis and a "fairness" discussion in an appraisal report is highly irregular. Graham and Albertini argue that when the report raises the issue of tax load and attempts to make a fairness claim, this suggests that the Stevens II was intended to produce a favorable valuation in favor of the Taxpayer, rather than an independent fee appraisal of value. Ex. 46. We cannot rely on the accuracy of that report. There is indication that potential bias colored the Stevens appraisal. Stevens I contains no mention of tax load as a part of assessed value or of equalization.

There is no mention of the Robert Lee property located on another island on Flathead Lake. There is no analysis or discussion of tax fairness. All these issues are first raised in Stevens II after the CTAB hearing, which found against the Taxpayer. Taxpayer is certainly entitled to prepare or change the case before this Board in any appropriate way, supplementing the record with relevant data or newly discovered material, adding or dropping claims. However, the fact that the revised report is heavily slanted in the Taxpayer's favor can only lead this Board to question its veracity as an independent appraisal of market value.

Stevens alleged that in his appraisal reports he regularly considers the overall "fairness" of the tax load. Tr. 127:3-12. He maintained that USPAP was silent as to whether discussion of over taxation was an appropriate part of any appraisal. Tr.127:13-17. Stevens admitted on cross-examination that his opinion that the subject property was "grossly overtaxed" had no bearing on the market value of the property to be determined through an appraisal. Tr. 200:1-5. He maintained though, that a discussion of taxes in an appraisal was appropriate and stated, "I do it in all my appraisal reports." Tr. 97: 18-25. He testified further: "[I] highlight it in all of my appraisal reports, not just this one, but all appraisal reports that I do." Tr. 98: 3-8.

The record directly contradicts Stevens' testimony about including tax burden analysis in his reports as a matter of course. Stevens I contains no such discussion or analysis of tax load or fairness in contrast with Stevens II. See Ex. 1; Cf. Ex. 28.

Stevens' equalization analysis does not prove that the DOR overvalued the subject property. The Stevens II report suggests that Taxpayer has been singled out and treated unfairly. The basis for this assertion is the report's comparison of the tax load on another property located on an island in Flathead Lake to the tax load of the subject property. Stevens II mischaracterizes equalization and how the DOR is required to equalize property in Montana.

Discussion of Taxpayer Contentions

Taxpayer avers numerous challenges to DOR's valuation. See "Evidence Presented" ¶ 20 (above). We begin by addressing the specific fact-related challenges to the DOR valuation.

The Taxpayer contends that "the [DOR] failed to meet the burden of "providing documented evidence to support its assessed values," citing *Trippet v. Mont. Dept. of Revenue*, 2012 WL 3870512. We find that the DOR market value is supportable by testimony and documentary evidence. Several reports and the preponderance of evidence submitted established the DOR's credibility

for the valuation. We find that even the construction cost data provided by the Taxpayer's accountant supports the DOR's cost methodology. This cost data is taken as admitted and established fact. However, construction costs alone are insufficient to determine valuation, without considering market factors. See e.g. *DeVoe*, 866 P.2d at 235; *Albright*, 933 P.2d at 822. The record shows that DOR considered market factors as well. *See* Tr. 705:19-706:5.

Therefore, we conclude that DOR has met the burden of credibly supporting the value assigned to the subject improvements. The Taxpayer has not met its burden of overcoming the presumption of correctness of the DOR market value. Given the cost estimates adduced by the Taxpayer, the uncontroverted testimony was that the direct job costs for the construction of the subject improvements were $35 to $37 million, and an additional cost of $19.7 million in indirect or other costs, leading to a grand total of $55 million. Given these costs, a valuation of $41 million seems a reasonable valuation for the subject, and is definitely not in the realm of "grossly overvalued" as was suggested by the Stevens II report. Ex. 1 at 00090.

Taxpayer contends the DOR appraiser was not qualified. We find that the appraiser was qualified to appraise the subject property. DOR residential and commercial appraisers are required to meet training and education standards. The DOR has promulgated an administrative rule to govern DOR's

certification of appraisers. The rule in salient parts states, "the DOR will develop policies and procedures outlining certification requirements that meet the International Association of Assessing Officers (IAAO) standards." (ARM 42.18.120.) Here the appraiser had relevant experience as an insurance adjuster for 20 years and additional IAAO sanctioned training while at the DOR in both commercial and residential appraising. Leuty has 20 years of experience in the private sector and 14 years of experience for the DOR appraising property of all kinds, including high value residential property. Prior to appraising the subject property, Leuty appraised twenty homes valued over five million dollars and a few over ten million dollars. See Evidence Presented ¶ 6 above. We find that the DOR appraiser possessed the necessary training and experience to appraise the subject property.

Taxpayer makes the assertion that the [DOR] failed to value the property at its market value as defined by statute. (M.C.A. § 15-8-111(a)and 15-8-111 (2). While the DOR must be able to explain and defend the proposed value, in tax appeals of property values, the burden is on the Taxpayer to overcome a presumption of correctness given to the DOR. *Farmers Union Cent. Exch. v. Department of Revenue*, 272 Mont. 471, 901 P.2d 561, 564 (1995); Western *Airlines, Inc. v. Michunovich*, 149 Mont. 347, 353, 428 P. 2d 3, 7, cert. denied 389 U.S. 952, 19 L. Ed. 2d 363, 88 S. Ct. 336 (1967.) As already explained in the

preceding discussion of the Taxpayer's case, we do not find the value argued or the methodology used by the Taxpayer to be credible enough to overcome the DOR's value.

Taxpayer contends DOR should have paid for an independent fee appraisal. We find no basis in law that requires the DOR to provide a fee appraisal on this property; therefore, this Board does not agree with this assertion. As part of its system of revaluation, the DOR adopted a comprehensive appraisal plan, as required by § 15–7–111, MCA. That plan was set forth in Rules 42.18.101[15] through 42.18.126, ARM. The Department's original appraisal plan provided that, for the first time, a Computer Assisted Mass Appraisal (CAMA) system would be implemented to assist the DOR's appraisers in the valuation process. *See Albright v. State By & Through State*, 281 Mont. 196, 199, 933 P.2d 815, 817 (1997). According to the DOR's original appraisal manual, adopted pursuant to Rules 42.18.123, ARM[16], the CAMA system is "designed to help the appraiser create and maintain records and procedures needed to arrive at a just, equitable, and defensible valuation for each parcel of real estate within [each] county" in the state. CAMA uses electronic files of property assessment data to help generate computer-assisted

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[15] These Administrative Rules are frequently repealed and revised for each re-appraisal cycle.
[16] The original manual was repealed and a new 2008 manual was adopted.

valuations for residential, agricultural, commercial, and industrial properties. The use of computer aided systems was upheld by the Montana Supreme Court in *Albright v. State By & Through State*, 281 Mont. 196, 199, 933 P.2d 815, 817 (1997). The CAMA system assists DOR's appraisers, provides standardized methods of valuation for fairness, and obviates the need to conduct an expensive independent appraisal on individual properties. More importantly, the legislature intended the DOR to use CAMA mass appraisal techniques in property valuation.

Taxpayer contends DOR's CAMA system was not adequate to find the value of this unique property. This Board has the task of determining adequacy of the DOR valuations. In this instance, the Taxpayer has failed to make a convincing case that the DOR value is not credible. Taxpayer claims the unique nature of the improvements should have excluded the subject property from mass appraisal techniques. Taxpayer failed to cite any statutory authority barring the DOR from using mass appraisal techniques to value this property. Montana law has not carved out an exception and has not precluded the uses of the CAMA system for unique or atypical properties. We find that the DOR's use of the CAMA system to value the subject property proper.

Taxpayer contends that DOR, in relying on actual costs provided by the Taxpayer himself, failed to take into account the significant additional costs

incurred resulting from building on an island. While there appears to be no requirement for this type of specific reduction, evidence and testimony in this case shows the DOR made substantial, multi-million dollar, reductions in value for a variety of reasons including cost overruns, and did make a reduction for depreciation. We find the DOR did consider the entirety of unique circumstances related to this property, including the island location, when it granted substantial valuation deductions during the informal review. This Board finds the DOR's substantial reductions granted during the informal review process adequately discounted for the indirect costs and the increase in costs due to the island location of this unique property.

Taxpayer contends that DOR failed to adequately discount for physical depreciation, functional obsolescence, and economic obsolescence. Taxpayer contends it was a fundamental failure of valuation to allow only a two percent reduction for depreciation. The two percent reduction on this property led to a downward value adjustment of $800,000. Any reduction in value on this new home seems to prove the DOR did consider and provide a reduction for depreciation. The DOR appraiser determined that, because the improvements were virtually brand-new, they did not need to apply a reduction of more than two percent to account for physical depreciation of the subject property. Tr. 584:3-10. This Board declines to replace the judgment of the DOR's appraiser

with its own judgment absent proof to the contrary of the extent of the functional and external obsolescence of the subject property.

Taxpayer presented credible evidence of additional obsolescence but this evidence was not sufficient to meet the Taxpayer's burden. *See Pacificorp* at ¶¶ 47, 48. The Taxpayer did not go far enough to prove how economic or functional obsolescence applied to the subject property. This Board finds Stevens' estimations of the economic and functional obsolescence speculative and unsupportable by the weight of the evidence. Taxpayer consistently argued that DOR underestimated obsolescence. It was Dr. Smith's opinion that the subject property, due to its one-of-a-kind nature and architectural uniqueness would not be desirable to potential buyers, especially high-net-worth individuals. His testimony speculated the existence of the diminution in value but did not quantify the extent of the Taxpayer's losses. Even if we take this reasoning as true, it is simply not enough on its own to meet the definition of either functional [17] or economic obsolescence[18] in the appraisal manual for the subject property. The condition causing functional obsolescence is generally

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[17] The Montana appraisal manual defines functional obsolescence as a condition caused either by inadequacies or over adequacies in design, style, composition, or arrangement inherent to the structure itself, which tends to lessen its usefulness (emphasis added). Montana Appraisal Manual at 17.

[18] The appraisal manual also defines economic obsolescence as a condition caused by factors extraneous to the property itself, such as changes in population characteristics and economic trends, encroachment of inharmonious land uses, excessive taxes, and governmental restrictions. Montana Appraisal Manual at 18.

incurable in that the causes lie outside the property owner's realm of control. *Id.* Taxpayer has alleged but not proved either economic or functional obsolescence by a preponderance of the evidence. The Stevens II report describes these categories of obsolescence but does not credibly explain how the subject property is directly affected. The Stevens reports and other testimony do not convince this Board by a preponderance of the evidence that the inadequacies or over adequacies in design, style, or composition lessen the subject property's usefulness.

The Taxpayer and DOR acknowledged that there was an economic downturn that affected the value of the subject property. Taxpayer and the Stevens reports do not prove by a preponderance of the evidence any "factors extraneous to the property itself, such as changes in population characteristics and economic trends, encroachment of inharmonious land uses, excessive taxes, and governmental restrictions," that may have lowered the value of this subject property. Stevens II also makes a blanket deduction of 30 percent for functional and economic obsolescence. See Evidence Presented ¶ 57. As discussed more fully above, how these percentages were calculated is rather opaque, unsupported by evidence, and unconvincing. Even if we take the economic recession as an established fact during 2008, the subject property is valued at the lien date of July 1, 2008. The Taxpayer has not adduced enough

evidence to convince this Board the short duration after the onset of the recession drastically affected the value of the subject property.

Dr. Smith suggested the existence of functional and economic obsolescence but did not credibly support his assertions with enough facts to show the extent and nature of the obsolescence with respect to this subject property. In this instance, the DOR appraiser determined that the improvements were brand new, and not affected by extraneous forces. The DOR appraiser thought it adequate to apply two percent depreciation. We find the discount applied is adequate absent credible evidence to the contrary.

Taxpayer contends that DOR failed to adjust its replacement cost analysis for "equal utility" as required by the Montana Appraisal Manual. This Board finds that it would be unreasonable for the DOR to value the two-foot thick custom-made stone walls of the subject property as the functional and economic equivalent of more typical stick-framed structures built with ordinary materials such as sheet rock. Taxpayer's argument here seems to advocate that a replacement value should be estimated by calculating a hypothetical house that replicates the subject improvements using only ordinary materials, ordinary designs, and ordinary construction labor. The Board finds that improvements built in this manner will not necessarily have "equal utility" to the subject property. The essence of the subject property and its utility necessarily derives

property. The essence of the subject property and its utility necessarily derives from its high quality of materials, its opulence, and its high-end finishes and high-level of skilled labor used to construct it. The testimony was uncontroverted that the finest materials from around the globe were used to construct this property and we find the taxable value of the property should reflect that quality.

Taxpayer contends that in valuing the property, the DOR failed to adjust the value to reflect the high cost of owning and operating the property. We find the DOR gave these costs the consideration they deserved when DOR calculated its replacement costs of the main house and the guesthouse by giving appropriate deductions as needed.

Taxpayer contends that the DOR failed to equalize the value of the subject property with other similarly situated properties. Further, Taxpayer alleges that the comparable properties used for valuation by DOR must represent similar properties within an acceptable proximity of the property being valued. Mont. Code Ann. § 15-8-111(3). The DOR appraiser testified that there were no comparable properties in its proximity. Taxpayer introduced the Lee property located on Cromwell Island as a proximate comparable property, though it had not sold. The DOR testified that the Cromwell property has never been completed and therefore could not be compared for

quality to the subject property.[19] The Montana Supreme Court has consistently stated that to obtain relief upon the ground that a Taxpayer's property is assessed inequitably, it is essential for a Taxpayer to show, at least: (1) there are several other properties within a reasonable area similar and comparable to the subject property; (2) the amounts of assessments on these properties; (3) the actual values of the comparable properties; (4) the actual value of the Taxpayer's property; (5) the assessment complained of; and (6) that by a comparison the Taxpayer's property is assessed at a higher proportion of its actual value than the ratio existing between the assessed and actual valuations of the similar and comparable properties, thus creating discrimination. *Mont. Dept. of Rev. v. State Tax App. Bd.*, 613 P.2d 691,694 (*cited in DeVoe*, 759 P.2d at 991.) Those criteria shall at least be a "starting place" for actual comparison of true value to assessed-value ratio. The discussion in *State Tax App. Bd. (cited above)* directed that the ratio system may be utilized if sufficient materials are presented by the DOR and the Taxpayer. See also DeVoe, 759 P.2d at 994. Given that this Board finds the Stevens appraisal value less credible and given the Board finds the Cromwell Island property is not a reasonable comparable property to the subject property, this Board cannot make a meaningful comparison under the test described above.

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[19] See discussion of the Lee property on page 55 of this opinion.

Taxpayer contends that contrary to established principles of "construction" [sic] law (we presume the Taxpayer meant constitutional law), the DOR singled out this Taxpayer for discriminatory or selective enforcement of the tax law. The Montana Constitution provides that, "no person shall be denied the equal protection of the laws." Mont. Const. art. II, § 4. "[T]axing authorities may not single out one Taxpayer for discriminatory, or selective, enforcement of a tax law that should apply equally to all similarly situated Taxpayers." *Penn Phillips Lands, Inc., v. State Tax Commn.*, 430 P.2d 345, 352 (Or. 1976).[20] The Board finds no credible evidence this Taxpayer was treated differently or denied equal protection. If anything, the use of CAMA system as already explained in our discussion ensures that all the Taxpayers in Montana are treated the same using mass appraisal techniques. Taxpayer may not agree with Montana law or tax policy. To change either, the remedy lies with the Montana Legislature, which writes Montana Law and sets tax rates, not this Board. The duty of this Board is to weigh the evidence presented to determine whether the value assigned to these improvements reflects true market value; we find a preponderance of the evidence supports the value assigned by the DOR to this property.

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[20] This Oregon case is cited by the Taxpayer.

The cost approach is generally used for residential property when comparable sales data is unavailable due to the uniqueness of the subject property or a lack of sales of comparable properties in the area. The cost approach is a determination of the current reproduction or replacement cost of improvements, less depreciation, plus the land value. *See generally* Appraisal of Real Estate; *See also* Montana Appraisal Manual, at 15; *See Albright*, 933 P.2d at 817-820. One function of the CAMA system is to apply the cost approach to valuation uniformly. CAMA applies the cost approach by determining the value of the underlying land, according to a computer-assisted land-pricing (CALP) estimation, Montana Appraisal Manual, at 461, and adding to that value the replacement cost of the improvements, minus depreciation as guided by Marshall and Swift Valuation Service or other depreciation schedules. *Id.* at 12; *See also Mont. Dept. of Rev. v. St. Tax App. Bd.*, 613 P.2d 691 (Mont. 1980) (discussing the DOR's use of Marshall and Swift manuals for appraising commercial properties). By statute, the Department of Revenue must "fully consider" a reduction in value for depreciation, including any physical, functional, or economic obsolescence. Mont. Code Ann. § 15-8-111 (2)(b); *see also Albright*, 933 P.2d at 822.

Construction costs alone, however, are insufficient to determine valuation without considering market factors. *See e.g. DeVoe*, 866 P.2d at 235;

Albright, 933 P.2d at 822. Taxpayer provided documentation of the construction costs, overruns, engineering mistakes, and other costs due to fraud. These costs standing alone are not determinative and may not be used in lieu of the market value of the subject property. We find the cost approach is an acceptable method to use for valuing the subject property, when coupled with accompanying market value support. See 15-8-111, MCA; *Albright*, 933 P.2d at 822. While there may have been additional market sales-based data available within or outside of Montana that an appraiser could have used when valuing the subject property, the DOR did consider a wide variety of available data sources for determining market value of the subject. The actual building costs provided to the DOR by the Taxpayer demonstrate or corroborate the fact that the DOR market value is within a defensible range of values.

Taxpayer contends that the DOR misapplied the cost approach to valuation by failing to develop a value for the property other than consideration of the actual costs of the project. We find the DOR did undertake and did verify the value arrived at by cost methodology with supplemental credible data from market sources. In addition, we find this effort was further supported by the fee appraisals introduced into this record. Actual costs were not the sole basis of the DOR valuation, but did in fact verify the range of value assigned to the subject property when compared to the fee appraisals.

Taxpayer asserted that at the CTAB hearing, DOR applied a capitalization of income method from a hypothetical source with no "back-up" data, and failed to justify its use. At the hearing before this Board, the Taxpayer asked if the DOR used the income approach in its valuation. DOR's appraisers testified that they did not use this valuation methodology to value the property but instead opted for the replacement cost new methodology also known as the cost approach. Tr. 615:11-617:4. We find that the income methodology was not used by DOR to determine the market value.

Taxpayer also alleged that the DOR presented inaccurate and irrelevant information through a marketing video at the county level. Taxpayer suggested that DOR used this marketing information in an improper manner in determining value. The record shows that this information was not used to inform the valuation process or methodology, nor was it presented at the hearing before this Board. This argument is unavailing and does not entitle the Taxpayer to a reduction in value.

Taxpayer contends that the DOR "relied upon" listing prices found on the internet. We distinguish between "relied upon," and "considered" in the totality of information used to determine the market value. We find the DOR considered other market data to support its value conclusion and did not rely on the listing prices to determine value.

Taxpayer contends that DOR's appraiser misapplied the concept of entrepreneurial profit in his valuation analysis and therefore failed to apply functional obsolescence and the factors commonly associated therewith. The property record card shows a discount for depreciation/obsolescence, and uncontroverted testimony indicates that discount at over $800,000. During the DOR's case-in-chief, the appraisers did not mention that they factored in any "entrepreneurial profit" in their valuation. More importantly, the Taxpayer did not adduce a modicum of evidence to support its allegation that the so-called "entrepreneurial profit," was used by the DOR to set value. Therefore, we do not find this contention to be credible.

Taxpayer contends the DOR's appraiser failed to extract market reactions from sales of higher priced properties in relation to their application of Reproduction Cost New (RCN) methodology. Taxpayer asserts further that market reactions method should be used as a measure of both functional and economic obsolescence. The Montana Appraisal Manual does not require market reactions to be used in the manner described by the Taxpayer here. Moreover, the DOR appraiser determined there were no comparable properties in the area. Therefore, the market reactions and data would not really affect the subject property if they indeed were not comparable to the subject

property. We find the appraiser relied upon the cost method as allowed by law, and supported his conclusion with credible market-based data.

The Taxpayer alleged that the DOR's appraiser and the appraisal prepared did not conform to the USPAP standards for mass appraisal of property for tax purposes. (Appeal Form attachment, Ex. A.) Based on our foregoing discussion of the DOR's appraisal we find the appraiser and appraisal met the standards required by Montana law.

Ultimately, we find that the DOR's assessment of Abbey's improvements is based on accepted valuation methodologies, and reflects fair market value as of the lien date. *See Albright v. State*, 281 Mont. 196, 933 P.2d 815 (1997.)

The Taxpayer challenged that Montana's property tax administration system was unfairly burdensome to him and was too costly. He argued that the tax burden is significantly higher than the burden placed on him for his California residence. If Williams' opinion is to be believed that a typical property owner in Montana pays 1.25 to 1.5 percent of the market value in property taxes whereas property owners of high-end, unique property such as the subject property pay only 1 percent of the market value in property taxes, then the Taxpayers' unfairness argument does not pass muster with the Board. Tr. 721:23-722:4. Williams estimates that Taxpayer is only paying .08 percent

in tax load compared to the market value of the subject property. Tr. 722: 1-4. Williams' opinion suggests that the Taxpayer has a lighter burden (considering the tax burden to market value ratio) than an average Montana property owner does. More importantly, this sort of public policy argument is not relevant to setting the market value.

The Taxpayer's building costs provided in the record demonstrate that the actual job costs of building the subject property were $37,266,973.08 based on Exhibit 32, a spreadsheet tabulating all the construction cost incurred. Further, Taxpayer's own testimony indicated that the subject property cost $35 million to construct. Tr. 339:1-8. Adding the direct job costs and other costs provided on the spreadsheet, the grand total cost becomes $55,512,373. The costs of the improvements are in line with the market value of the house most similar to the subject property, the Two Bear property near Whitefish. See Evidence Presented ¶ 36. Williams testified that the Two Bear property was a similar property for valuation purposes, and that the value of that property was approximately $38 million. *Id.* Finally, we note that this valuation is also in line with both fee appraisals in the record. These appraisals have not been time trended back to the lien date and therefore are not properly before us for determining value, but do allow this Board to consider them as corroborating evidence of market trends and as benchmarks of the reasonableness of the

DOR value. *Puget Sound v DOR* (CT-2007-5; June 2009). We find the DOR appraiser appropriately considered the national market and other relevant information including the listing prices of the subject property in assessing the reasonableness of their appraised market value. Section 15-7-102(6), MCA, expressly authorizes [the Board] to "consider the actual selling price of the property, independent appraisals of the property, and other relevant information" in determining the market value of the property. *See generally Pacificorp*, ¶ 57. In this instance, both of the fee appraisals of the property lend credence to the DOR value assigned. Note that the Taxpayer voluntarily made these appraisals a part of the record before this Board. Neither the DOR nor this Board relied upon the market values found in these independent appraisals to derive the value of the subject property. However, as part of the evidence presented this Board found them credible as a supporting source of market based data to uphold the value assigned by the DOR. These appraisals were considered for the sole purpose of verifying a market value.

Thus, we find that the DOR valuation using the cost approach is credible, and supported by market information allowed by 15-8-111, MCA.

Conclusion

The Board affirms the assessed value as modified by this Board.

Order

IT IS THEREFORE ORDERED by the Montana Tax Appeal Board that the Department of Revenue apply a two percent depreciation factor to the main residence and enter the new appraised value on the tax rolls of Lake County accordingly.

Dated this 18th day of March 2015.

BY ORDER OF THE
MONTANA TAX APPEAL BOARD

DAVID L. McALPIN, Chairman

(SEAL)

STEPHEN A. DOHERTY, Member

VALERIE A. BALUKAS, Member

Notice: You are entitled to judicial review of this Order in accordance with Section 15-2-303(2), MCA. Judicial review may be obtained by filing a petition in district court within 60 days following the service of this Order.

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on this 18th day of March, 2015, the foregoing Order of the Board was served on the parties hereto by depositing a copy thereof in the U.S. Mail, postage prepaid, addressed to the parties as follows:

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