

06-0724

CENTRALLY ASSESSED PROPERTY

TAX YEAR: 2006

SIGNED: 03-19-09

COMMISSIONERS: P. HENDRICKSON, R. JOHNSON, M. JOHNSON, D. DIXON

GUIDING DECISION

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER, Petitioner, v. PROPERTY TAX DIVISION OF THE UTAH STATE TAX COMMISSION, Respondent, SALT LAKE COUNTY, Intervener.	FINDINGS OF FACT, CONCLUSIONS OF LAW AND FINAL DECISION Appeal No. 06-0725 Tax Year: 2006 Tax Type: Centrally Assessed Property Judge: Phan
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This Order may contain confidential “commercial information” within the meaning of Utah Code Sec. 59-1-404, and is subject to disclosure restrictions as set out in that section and Utah Admin. Rule R861-1A-37. The rule prohibits the parties from disclosing commercial information obtained from the opposing party to nonparties, outside of the hearing process. However, pursuant to Utah Admin. Rule R861-1A-37 the Tax Commission may publish this decision, in its entirety, unless the property taxpayer responds in writing to the Commission, within 30 days of this order, specifying the commercial information that the taxpayer wants protected.

Presiding:

Pam Hendrickson, Commission Chair
Bruce Johnson, Commissioner
Marc Johnson, Commissioner
D’Arcy Dixon Pignanelli, Commissioner
Jane Phan, Administrative Law Judge

Appearances:

For Petitioner: PETITIONER REP 1, Attorney at Law
 PETITIONER REP 2, Attorney at Law
For Respondent: RESPONDENT REP, Assistant Attorney General
For Intervener: INTERVENER REP 1, Deputy District Attorney
 INTERVENER REP 2, Attorney at Law

STATEMENT OF CASE

This matter came before the Utah State Tax Commission (“Commission”) for a Formal Hearing on September 29, 2008, through October 1, 2008, pursuant to the provisions of Utah Code Secs. 59-2-1007 & 63G-4-2-1 et seq. Petitioner PETITIONER (“PETITIONER”) had filed an appeal of the Notice of Assessment issued by the Property Tax Division (the “Division”) dated March 28, 2006, in which the Division assessed a system value for PETITIONER’s operating property of \$\$\$\$ as of January 1, 2006. After vehicle adjustments and the adjustment for the federal Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), the Utah assessment was \$\$\$\$ (“Original Assessment”).¹

Salt Lake County (the “County”) did not file an appeal of the Division’s Notice of Assessment, but was granted intervenor status prior to the scheduled Formal Hearing. During the course of the Formal Hearing, the County filed a Motion for Directed Verdict, which was not granted at that time and to which the parties were allowed to respond in posthearing filings. Based on those filings, and as addressed further below, the Commission denies the Motion herein. Posthearing and reply submissions were filed by each party and the County, on or prior to December 31, 2008, which the Commission considered prior to the issuance of this decision.

Based upon the oral and written pleadings, as well as the evidence, testimony, and exhibits presented at the Formal Hearing, the Commission makes and enters its:

FINDINGS OF FACT

1. The property that is the subject of the assessment at issue is the taxable operating property of PETITIONER, as of the lien date January 1, 2006.

2. The Division classifies airlines into various categories. The Division considered PETITIONER to be in the (X) category or market. PETITIONER flies to (X) states in the United States.²

3. (PARAGRAPH REMOVED)

4. (PARAGRAPH REMOVED)

5. (PARAGRAPH REMOVED)

6. In determining PETITIONER’s Utah property assessment for tax year 2006, the Division did consider several value indicators in its Original Assessment. The Division had prepared a cost indicator of \$\$\$\$\$, an income indicator of \$\$\$\$\$, a stock & debt market indicator of \$\$\$\$\$, an Airliner

¹ See Petitioner’s Exhibit 1.

Price Guide (“APG”) Retail market indicator of \$\$\$\$ and an APG Wholesale market indicator of \$\$\$\$\$. The Division then placed 100% of the weight on the APG Wholesale indicator, which resulted in a reconciled system value rounded of \$\$\$\$\$. The Division concluded that the appropriate interstate allocation factor for Utah was 1.01%, which it applied to the reconciled system value. After deduction for locally assessed vehicles, this resulted in a Utah taxable value of \$\$\$\$\$.³ This value was further reduced by 6.43% for TEFRA, resulting in the Utah assessment value of \$\$\$\$.

7. In the income indicator in its original assessment, the Division had capitalized normalized net operating income (“NOI”) in the amount of \$\$\$\$\$. Because the Division was looking to capitalize NOI, the Division had not considered Deferred Income Tax (“DIT”) in the equation. The Division capitalized the normalized NOI by a rate of %%%%. The Division subtracted zero for growth in determining the rate.⁴

8. Placing all of the weight on the APG Wholesale indicator was consistent with how the Division had valued all other airlines in the original 2006 airline assessments.⁵

9. On or about June 24, 2008, the Division prepared an appraisal of the subject property for the January 1, 2006, lien date (the “Second Appraisal”). APPRAISER A, Senior Appraiser, Property Tax Division, prepared the Second Appraisal and it was APPRAISER A’s conclusion in this appraisal that the reconciled system value was \$\$\$\$ and the Utah taxable value was \$\$\$\$\$.⁶ There were several differences between the Second Appraisal and the Original Assessment. APPRAISER A had made corrections to the income approach. He capitalized cash flow rather than NOI and deducted an inflationary growth of 2.40% from the cost of capital of %%%%, which he had increased from the cost of capital of %%%% used in the Original Assessment. There was also a small correction to the Stock and Debt indicator. However, the primary difference, the one that ultimately affected the value, was that APPRAISER A placed 100% weight on APG Retail value, while the Original Assessment had 100% of the weight on APG Wholesale.⁷

10. After the Second Appraisal had been issued, PETITIONER discovered that it had made a

² Hearing Transcript, pg. 677.

³ Petitioner’s Exhibit 1, pg. 6.

⁴ Petitioner’s Exhibit 1, pg. 9.

⁵ Hearing Transcript, pg. 280.

⁶ Petitioner’s Exhibit 2.

⁷ Hearing Transcript, pgs. 203-207.

reporting error on its 2006 Annual Property Tax Report regarding the age of (X)of its airplanes. When this was pointed out to the Division, the Division revised its Second Appraisal by correcting the ages and calculating the corresponding change in value. This correction was prepared by APPRAISER A and was dated August 21, 2008 (“Revised Appraisal”).⁸ The only difference between the Second Appraisal and the Revised Appraisal was the change resulting from PETITIONER’s reporting error.⁹ At the hearing the Division asked that the value be raised to the value established in the Revised Appraisal.

11. A comparison of the differences between the Division’s Original Assessment and Revised Appraisal are as follows:

	Division’s Original Assessment¹⁰	Division’s Revised Appraisal¹¹
Income		
DIT Added in CF	No	No
Income Stream	NOI	Cash Flow
Income Capitalized	\$\$\$\$\$	\$\$\$\$\$
Cost of capital	%%%%%	%%%%%
Growth	0	%%%%%
Capitalization Rate	%%%%%	%%%%%
Income Value	\$\$\$\$\$	\$\$\$\$\$
Plus Leases	\$\$\$\$\$	\$\$\$\$\$
Minus Software	(\$\$\$\$\$)	(\$\$\$\$\$)
Income Indicator	\$\$\$\$\$	\$\$\$\$\$
Cost		
Total Value	\$\$\$\$\$	\$\$\$\$\$
APG Market		
Column	Wholesale	Retail
Value	\$\$\$\$\$	\$\$\$\$\$
Stock & Debt		
Total Stock & Debt	\$\$\$\$\$	\$\$\$\$\$
Plus Curr. Liabilities	\$\$\$\$\$	\$\$\$\$\$
Less Curr. Assets	(\$\$\$\$\$)	(\$\$\$\$\$)
Operating Property Allocation	82.19%	82.19%

⁸ Petitioner’s Exhibit 3.

⁹ Hearing Transcript, pg. 205.

¹⁰ Petitioner’s Exhibit 1.

¹¹ Petitioner’s Exhibit 3.

Plus Leases	\$\$\$\$\$	\$\$\$\$\$
Less Exempt Software Value	99.31% \$\$\$\$\$	99.31% \$\$\$\$\$
Weighting	100% APG Wholesale	100% APG Retail
System Value	\$\$\$\$\$	\$\$\$\$\$
Interstate Allocation	%%%%%%%%	%%%%%%%%
Utah Taxable	\$\$\$\$\$	\$\$\$\$\$
TEFRA Reduction	%%%%%%%%	%%%%%%%%
Assessment	\$\$\$\$\$	\$\$\$\$\$

12. Neither PETITIONER nor the County submitted an appraisal at the hearing.

13. It was the County’s position that the Commission should adopt the Division’s Revised Appraisal value.

14. It was PETITIONER’s position that there was error in the Division’s Original Assessment and in the Division’s Revised Appraisal and that there was basis to indicate a lower value. PETITIONER asked that 100% of the weight be placed on an income indicator corrected for 0 growth, or if weight is to be given to the APG, 50% weight should be given to APG Wholesale minus an additional fleet discount and the remaining 50% to the corrected income indicator.¹²

15. The issues that arose from the evidence and argument presented at the hearing were whether the Commission should add DIT to the cash flow, whether the Commission should make a modification to the Division’s growth factor in capitalization rate, or consider a modification of the capital structure, whether the Commission should place weight on indicators other than the APG and if weight is placed on the APG, whether APG Wholesale or APG Retail should be considered.

The Division’s Income Indicator.

16. **DIT in the Cash Flow:** When he prepared the Revised Appraisal, APPRAISER A did not add the \$\$\$\$\$ of DIT in the cash flow. He testified that he had done this based on his understanding of a Tax Commission decision from another appeal, Tax Commission Findings of Fact, Conclusions of Law and Final Decision, Appeal No. 06-0767 & 06-0773, (“Decision in Appeal No. 06-0767”). In that decision the Tax Commission had determined that DIT should be offset by capital expenditures, but that appeal involved a mature, cost regulated utility. After preparing the Revised Appraisal and after

¹² Hearing Transcript, pg. 683.

reviewing other subsequent decisions from the Tax Commission, APPRAISER A concluded that the Commission's Decision in Appeal No. 06-0767 would not apply to airline property. It was APPRAISER A's testimony that he now felt DIT should have been added in the cash flow, and further, that adding DIT to the cash flow would comply with Utah Administrative Rule R884-24P-62.¹³

17. WITNESS A, Manager of Property Tax, PETITIONER, testified that PETITIONER filed tax returns in (X) states.¹⁴ WITNESS A acknowledged that other states included DIT in the cash flow and that it was required by rule.¹⁵ She testified that she had previously agreed that DIT should be added before she heard about the Decision in Appeal No. 06-0767 and if that decision did not apply to airlines then she agreed that this adjustment should be made to the income indicator.¹⁶ However, APPRAISER B, MAI, CAE and Certified General Appraiser, testified it was his opinion that in a no growth scenario, the DIT should not have been added.¹⁷

18. It is the Commission's conclusion that in this matter the DIT should have been added in the cash flow. The Division apparently misunderstood the Tax Commission's intent in its Decision in Appeal 06-0767 at the time that the Revised Assessment had been prepared. That decision was based on the testimony and evidence submitted for that hearing regarding a mature, cost regulated utility. The Commission would not apply that decision on DIT for an airline absent the same type of showing that had been made by the cost regulated entity.

19. **Growth:** It was PETITIONER's position that the Division had erred in its appraisal by subtracting 2.4% for growth from its cost of capital of %%%%. This resulted in a capitalization rate of %%%%. APPRAISER A explained that he had subtracted 2.4%, as that was his estimate of the inflation rate. It was his position that this amount should be subtracted as directed by Rule 62.¹⁸ He did note that he considered the appraisal to be a no growth perspective because he had estimated capital expenditures to equal the sum of depreciation expense plus amortization.¹⁹

20. PETITIONER argued that the appropriate rate for growth was 0. PETITIONER's representative, WITNESS A, calculated that if 0 growth were applied in the Division's Revised

¹³ Hearing Transcripts, pgs. 126-127, 217.

¹⁴ Hearing Transcript, pg. 676.

¹⁵ Hearing Transcript, pg. 653-654.

¹⁶ Hearing Transcript, pgs. 653-654, 670.

¹⁷ Transcript, pgs. 568-569.

¹⁸ Hearing Transcript, pg. 132.

Appraisal, this would raise the capitalization rate to %%%%. WITNESS A calculated that when this rate was applied to the Division's cash flow in the Revised Appraisal of \$\$\$\$ and the same software adjustments were made as had been done by the Division, this would result in an Income Indicator value of \$\$\$\$\$. If 100% of the weight was placed on this indicator, it was WITNESS A's conclusion that the Utah assessment would be reduced to \$\$\$\$ or \$\$\$\$ after the TEFRA adjustment.²⁰

21. Regarding the growth rate, WITNESS A testified that she was not comfortable with a growth factor in the capitalization rate.²¹ She had acknowledged that she was not an appraiser, however. She pointed out that the 0 growth rate was similar to the Division's income approach in the Original Assessment, which had resulted in a similar number to what WITNESS A was requesting for PETITIONER.²² In requesting the 0 growth rate, she also relied on the opinion of APPRAISER B. She did not perform other independent analysis.²³ Further, she did not know if the Division's growth rate was consistent with PETITIONER's business plan. She did not consult with PETITIONER's management regarding appropriate capital expenditures or what they planned to earn into perpetuity.²⁴

22. APPRAISER B testified at the hearing regarding his opinion on the growth rate but would not give an opinion on whether his suggested change resulted in the correct capitalization rate. APPRAISER B pointed out that APPRAISER A had claimed the Revised Appraisal was prepared based on a 'no growth' perspective. It was APPRAISER B's opinion that in a no growth perspective you cannot have a growth rate. APPRAISER B testified, "G is equal to zero in this case. It has to be." "That means automatically that the rate of return climbs upward into infinity. That is not possible in a competitive airline arrangement. It's just simply not possible." However, APPRAISER B made it clear that he was not offering an opinion of value in this matter and would not state if he thought that the Division's value was too high or too low.²⁵ Nor did he offer an opinion that the %%%% capitalization rate which results from 0 being subtracted for growth was the correct answer, but it was his position that to correct what he saw as a fundamental flaw in the theory of the Division's Revised Appraisal, growth

¹⁹ Hearing Transcript, pg. 120.

²⁰ Petitioner's Exhibit 4.

²¹ Hearing Transcript, pg. 652.

²² Hearing Transcript, pg. 674, Petitioner's Exhibit 1.

²³ Hearing Transcript, pg. 674.

²⁴ Hearing Transcript, pgs. 666-667.

²⁵ Hearing Transcript, pgs. 587, 589, 605-606.

would need to be 0.²⁶ However, APPRAISER B did acknowledge that revenues would increase by inflation in nominal dollars, that there were efficiencies that might create growth in the short term and it was possible that PETITIONER could expand to new markets with the existing assets.²⁷

23. Upon reviewing and weighing the evidence presented on the growth rate, the Commission declines to make the change to \$0 growth as argued by PETITIONER. As noted by the Division, APPRAISER B, the one appraisal witness for PETITIONER, is picking one of a number of the components of the capitalization rate and arguing that it should be changed in PETITIONER's favor, but then refusing to give an opinion that if that one change is made the result is the correct capitalization rate. Certainly there could be changes to the other components of the capitalization rate that would result in a higher value, for example a change in the capital structure. However, APPRAISER B is choosing to argue only regarding the one component, the growth factor, without assurance that the result is the correct capitalization rate. The Division had determined the rate from studies of the various components, concluded that an inflationary growth should be subtracted from the cost of capital and that this was necessary for compliance with Rule 62. Furthermore, the Commission does not accept APPRAISER B's premise that the rate of return climbs upward into infinity. The Commission does not agree with APPRAISER B's interpretation of the yield capitalization model, which inherently recognizes changes in growth patterns as well as a termination value. APPRAISER B failed to provide a convincing alternative analysis to prove that the Division's estimate of growth was incorrect.

24. **Capital Structure:** During the course of the hearing, the Division's representative, APPRAISER A, questioned the capital structure he had used to develop his cost of capital in the income indicator. APPRAISER A testified that he had used the capital structure that resulted from PETITIONER being included in the average for the (X) airline category of the Division's Capitalization Rate Study.²⁸ He testified that PETITIONER's capital structure was nearly %%%% equity and %%%% debt. (SENTENCE REMOVED)

25. Adding PETITIONER with the other (X) airlines resulted in an average of 75% equity and 25% debt, which is what APPRAISER A, had used in his appraisal.²⁹ (SENTENCES REMOVED)

²⁶ Hearing Transcript pg. 568.

²⁷ Hearing Transcripts, pg. 599.

²⁸ Respondent's Exhibit 8.

²⁹ Petitioner's Exhibit 3, pg. 13.

However, APPRAISER A also had other concerns with the capital structure, including the trend in the industry that airplanes were being financed by operating leases. APPRAISER A did not recommend making the change in the capital structure, but instead argued that to account for this and other concerns with his income approach, no weight should be given to his income indicator.

26. The Counties argued that if the capital structure was changed to %%% equity and %%% debt, (PORTION REMOVED); the result would be a higher value for the subject. The County had APPRAISER A calculate the value making the change to the capital structure and the DIT correction. APPRAISER A's determination with these two changes was a value of \$\$\$\$.³⁰ This change was not directly advocated by any of the witnesses in this matter. APPRAISER A had noted concerns with the capital structure and concerns regarding operating leases, but in the end had used the 75% equity and 25% debt structure in his appraisal.³¹ The evidence was insufficient to support the change in capital structure argued by the County. (SENTENCE REMOVED). There is no evidence to conclude that PETITIONER's earnings would be the same with a different capital structure.

APG Retail versus APG Wholesale Indicators

27. In the Original Assessment the Division had considered the other indicators, but had valued PETITIONER by placing 100% of the weight on the APG wholesale indicator. This resulted in a system value for PETITIONER of \$\$\$\$.³²

28. After PETITIONER had filed an appeal of the assessment, the Commission heard a valuation case involving another airline, which was not PETITIONER or related to PETITIONER. The Commission issued its decision in that appeal, Tax Commission Findings of Fact, Conclusions of Law, and Final Decision, Appeal Nos. 06-0768 & 06-0740, on August 28, 2007 ("Prior Airline Decision"). APPRAISER A testified that the Division concluded from the Tax Commission's Prior Airline Decision, as well as the testimony of WITNESS B, who is the (X)of the Airliner Price Guide or APG, given during those proceedings, that the appropriate APG factor to use for PETITIONER and other airlines was not the APG Wholesale, but was, instead the APG Retail.³³

29. For the Revised Appraisal the Division placed 100% weight on APG Retail. This one

³⁰ Hearing Transcript, pg. 241.

³¹ Petitioner's Exhibit 3.

³² Petitioner's Exhibit 1.

³³ Hearing Transcript, pgs. 150-152.

change accounts primarily for the increase in value from the \$\$\$\$ system value in the Original Assessment to the \$\$\$\$³⁴ system value of the Revised Appraisal. The Division had taken the APG Retail value, without any adjustment, for each aircraft in PETITIONER's fleet. The Division then added that value to its cost value of the nonmobile assets of PETITIONER to determine its APG Retail indicator of value.

30. Unlike the subject appeal, in the Prior Airline Decision, the issue the parties presented at the hearing was limited to whether the valuation should be based on APG Wholesale or APG Retail. The issue of whether or not other valuation indicators should have been given more weight was not raised, and, therefore, not addressed by the Commission in that decision.³⁵ In the appeal that is the subject of this decision, what weight, if any, should be placed on the APG and on other indicators of value are issues directly raised by PETITIONER and upon which testimony was offered.

31. The Airliner Price Guide, or APG is published by COMPANY A, and is a valuation guide to value single airplanes or several airplanes sold in a single transaction. WITNESS B testified at the Formal Hearing in this matter that the values contained in the APG are intended to estimate the current market value for an average aircraft of any particular type that is typically configured and in half-time condition.³⁶

32. WITNESS B explained the different use intended for the Retail versus Wholesale Columns of the APG. He testified that the Retail Column is to assist in determining the value when the sales transaction involves from one to three aircraft. Once the transaction involves a fourth aircraft then it is intended that the Wholesale Column be used because the buyer would expect to receive a discount. "So the wholesale column is intended to account for the fact that if someone's buying more than four, four or more, that the value may be less."³⁷ Further the guide indicated there would be an additional fleet discount applied when the transaction involved a larger number of airplanes sold at one time.

33. WITNESS B clarified that the APG is not an appraisal of any specific airline, that you would not use the APG as the sole basis for conducting an appraisal, that the APG would be one of the data points. He testified, "The Airliner Price Guide is not an appraisal book. You would not use that

³⁴ Petitioner's Exhibit 3.

³⁵ Tax Commission, Findings of Fact, Conclusions of Law, Final Decision, Appeal Nos. 06-0768 & 06-0740.

³⁶ Hearing Transcript pgs. 329-330.

³⁷ Hearing Transcript, pg. 371.

book as the sole basis for conducting an appraisal. It would be one of the data points . . .”³⁸

34. The evidence and testimony submitted in this matter was that the APG was designed to provide a starting point to value a single aircraft or purchase of a small number of aircraft, that there was market validation for this particular purpose.³⁹

35. However, the testimony at the hearing from the various experts and witness indicated that the APG is not a unitary valuation method for an operating airline. WITNESS B himself made this point. He testified that the APG was just a guidebook, that it was not an appraisal, that he did not consider USPAP or Utah law in preparing the guidebook. When asked if he intended the values contained in the APG to be used for the purpose of a unitary assessment of an airline’s fleet of aircraft, WITNESS B answered, “I don’t know and I didn’t do that. I’m not familiar with unitary assessment procedures.” The questioner went on to ask if PETITIONER might be sold as an entire operating unit in a corporate transaction, which WITNESS B acknowledged was possible, but that was not what he did in the APG.⁴⁰

36. WITNESS C, (WORDS REMOVED), and Expert Witness in matters of unitary valuation, testified in regards to the APG that it was a summation approach,⁴¹ that it was designed to value a single plane or several planes, not entire fleets.⁴² APPRAISER B also testified that the APG is not a unitary appraisal concept, that it was a summation concept.⁴³ It was his testimony regarding the APG as follows: “The concern is briefly this: Complete reliance on the information in the Airliner Price Guide, plus the net book value of non-aircraft types of assets I think would be improper in this situation unless you can test it by some unitary concept, and since this is not really a unitary concept, I think we found abundantly clear in USPAP that you have to be really careful in just simply summing up appraised values or net book values and expecting the whole to equal the sum of these parts.”⁴⁴ He also indicated that a real market or sales indicator of value for an operating airline would be based on a sale of an operating airline, not the sale of airplanes.⁴⁵

³⁸ Hearing Transcript, pg. 399.

³⁹ Hearing Transcript, pgs. 526-527.

⁴⁰ Hearing Transcript, pg. 344-355.

⁴¹ Hearing Transcript, pg. 494.

⁴² Hearing Transcript, pgs. 525-526.

⁴³ Hearing Transcript, pg. 614.

⁴⁴ Hearing Transcript, pg 570.

⁴⁵ Hearing Transcript, pg. 576.

37. In addition to concerns that the APG did not provide a unitary value for an operating airline, witnesses for PETITIONER testified that they had concerns regarding the lack of transparency of the sales information that was relied on by WITNESS B and his company to determine the values indicated in the APG. WITNESS B considered much of his sales information to be confidential and had not produced it on that basis during the discovery phase or during testimony at the hearing. APPRAISER B noted that an appraiser should be cautious about relying solely on the work of another. WITNESS C noted that an appraiser should not place total reliance on the work of another without adequate disclosure.⁴⁶

38. The parties disagree on how the APG should be applied. The Division and the County argued the indicator should be the APG Retail, while PETITIONER argued for APG Wholesale minus a fleet adjustment. The arguments and the testimony presented at the hearing demonstrate the difficulty in relying on a non-unitary valuation method to determine the unitary value of an operating airline.

39. WITNESS C argued that the APG Wholesale should be used. It was his contention that each additional airplane sold would decrease the value. He offered that an absorption rate should be applied and the larger number of aircraft sold the larger the discount should be. When pressed he indicated that in this matter the discount would be somewhere less than %%%%.⁴⁷ However, as noted by the Division and the Counties, WITNESS C's analysis fails to take into consideration the unit being valued is an operating airline not airplanes.

40. The testimony from WITNESS B, who all parties acknowledge was the expert on how his guidebook should be applied,⁴⁸ demonstrates to the Commission that it cannot rely on either the Retail or the Wholesale value to apply uniformly as a valuation technique for all airlines, because the value of an operating airline will depend on the financial condition of the airline. WITNESS B testified that if PETITIONER was selling (X) plus airplanes you would expect a discount. However, if they were selling the entire operating company, the sale could be for higher than APG Retail for the aircraft because the buyer would pay a premium.⁴⁹ He went on to testify, "Generally speaking, if you were

⁴⁶ Hearing Transcript, pgs. 467-468.

⁴⁷ Hearing Transcript, pgs. 460, 470-471, 492-493.

⁴⁸ Hearing Transcript, pg. 673.

⁴⁹ Hearing Transcript, pg. 353-354.

selling an entire entity, you could indeed achieve a higher value based upon the success of the airline.”⁵⁰ He further clarified a corporate sale may be higher, lower or the same as a bulk sale.⁵¹

41. An appraisal was submitted in this matter that had been prepared by COMPANY B (COMPANY B) at the request of the Division to value PETITIONER’s property for the 2004 tax year (“2004 COMPANY B Appraisal”).⁵² (SENTENCE REMOVED). The appraisal refers to an undefined term of ‘market value,’ but does not reference ‘fair market value,’ or components of the definition of ‘fair market value’ including willing buyer and willing seller. The appraisal states that it is a “valuation opinion for each aircraft” and [a]ccording to values contained within the Airliner Price Guide.” It describes its conclusion as ‘total market value.’⁵³ The value for the airline was determined in the COMPANY B appraisal by summing the value of each aircraft according to the retail column of the APG. This is the same manner used by the Division to determine its Market Indicator in the Revised Appraisal.

42. The Commission is concerned with the use of the APG for reasons presented by the expert witnesses. Based on this testimony, the Commission can only conclude that it is merely coincidental if the values of the each individual airplane summed either under the APG Retail or APG Wholesale Column plus the book value of the nonmobile assets results in a value near the fair market unitary value of the airline itself. Whether the value of the operating airline is nearer retail or nearer wholesale will depend on the profitability of the airline. Therefore, the Commission cannot make a finding that uniformly, for all airlines, APG Retail would be a better valuation method to apply than APG Wholesale. The APG is simply not a method of unitary valuation.

43. The Commission does recognize that the APG presents a means for uniform assessments among airlines based on the type and age of the airplanes, and may in fact present a benchmark for analyzing other value indicators. In extreme cases, if it were shown a complete absence of another meaningful approach to valuing an airline, the Commission may consider the use of the APG as a proxy. However, for PETITIONER there is another meaningful valuation indicator, that being the income indicator. (SENTENCE REMOVED). Despite this, the income indicator is supporting a value more

⁵⁰ Hearing Transcript, pg. 390.

⁵¹ Hearing Transcript, pg. 391.

⁵² Petitioner’s Exhibit 41.

⁵³ Petitioner’s Exhibit 41, pg. 4.

closely aligned with APG wholesale, not APG retail.

44. **Weighting of Indicators.** PETITIONER asks that 100% of the weight be placed on the income indicator corrected for 0 growth. However, PETITIONER asks that if the Commission were to determine that some weight should be given to an APG indicator, at least 50% be given to the income indicator and the remaining 50% given to the APG Wholesale with an additional fleet discount. The Division and the County argue that 100% of the weight should be given to the APG Retail indicator.

45. Although he gave them no weight, APPRAISER A for the Division had prepared unitary valuation indicators including those indicators derived by the preferred methods set out in Rule 62, which are a cost method and the yield capitalization income method. The Division points out that the APG Retail of \$\$\$\$ was well within the range of the other indicators. In the Revised appraisal, the highest indicator of value was the Stock & Debt indicator of \$\$\$\$ while the lowest was the income indicator of \$\$\$\$ (uncorrected for DIT). The cost indicator at \$\$\$\$ was higher than APG Retail. APG Wholesale, upon which the Division placed 100% of the weight in the Original Assessment, was lower at \$\$\$\$.

46. The Division's appraiser, APPRAISER A, acknowledged that there was some obsolescence in his cost indicator and testified that he took the obsolescence into account by giving the indicator no weight.

47. APPRAISER A's stock and debt indicator, which is a unitary method, was at \$\$\$\$\$. This is substantially higher than any other indicator, suggesting that the value may be capturing more intangibles than the preferred methods. APPRAISER A indicates that he did not place weight on this indicator based on the fact that the Tax Commission historically has given this indicator little weight.

48. APPRAISER A testified that he was not comfortable placing any weight on the income indicator. He noted that he was fairly comfortable with the normalized NOI for the 2006 year, for PETITIONER.⁵⁴ However, he felt that DIT should have been added as part of the cash flow and if added, it was his opinion that his income indicator would comply with Rule 62.⁵⁵ He did have concerns with his capitalization rate, and argued that this was one of the reasons that he placed no weight on the income indicator. (SENTENCES REMOVED) He testified that he valued all airlines for the 2006 year based on the APG for a uniform and equal assessment.⁵⁶

⁵⁴ Hearing Transcript pg. 122-124.

⁵⁵ Hearing Transcript pg. 134.

⁵⁶ Hearing Transcript, pgs. 236-237.

49. PETITIONER argued that all, or at least 50% of the weight should be placed on the income indicator. PETITIONER presented testimony from WITNESS D, Director of the Property Tax Division. WITNESS D testified that generally the income approach should be the primary indicator of value for an income producing property.⁵⁷ WITNESS D indicated that he thought it had not been used in this matter due to uniformity considerations.⁵⁸ WITNESS C, testified that “the income indicator of value is a very important indicator of value and should be relied upon” for income producing properties.⁵⁹ He further testified that he would give most of the weight in the Division’s Revised Appraisal to the income approach and very little weight to the other indicators.⁶⁰

50. After consideration of all the evidence in this matter, it is the Commission’s conclusion that the best indicator for valuing the subject property is the yield capitalization income indicator. This conclusion is based not only on the fact that the yield capitalization method is a preferred unitary appraisal method under Rule 62, but also from the testimony of the witnesses at the hearing who were persuasive in arguing that the income indicator was a viable unitary method for valuing the subject property and that the APG was not a unitary method. With DIT of \$\$\$\$ added, the income capitalized is \$\$\$\$. Applying the cost of capital of %%% and a growth rate of %%% results in a capitalization rate of %%%. Capitalizing the cash flow by this percentage equals \$\$\$\$\$, to which \$\$\$\$ is added for the leases and an adjustment made for the exempt intangibles. The result is a system income indicator of \$\$\$\$\$. From the evidence presented in this matter, the Commission concludes that 100% of the weight should be placed on this indicator.

51. Applying the Utah allocation factor of 1.01% to the system indicator of \$\$\$\$\$ results in a Utah property valuation of \$\$\$\$\$. Subtracting registered motor vehicles at fair market value in the amount of \$\$\$\$\$ equals a Utah taxable value of \$\$\$\$\$. From the Utah taxable value, a %%% reduction is made for TEFRA. Subtracting this amount results in a Utah assessment of \$\$\$\$\$. The Commission concludes that the Utah assessed value after the TEFRA adjustment is the \$\$\$\$\$.

52. With respect to the Stock and Debt indicator, the Commission recognizes it as an appropriate method for business valuation purposes and with appropriate adjustments, it can be used for

⁵⁷ Hearing Transcript, pgs. 64-65.

⁵⁸ Hearing Transcript, pg. 70.

⁵⁹ Hearing Transcript, pg. 457, ln. 6.

⁶⁰ Hearing Transcript, pg. 523.

unitary property appraisal. However, the Commission traditionally gives little or no consideration to the Stock and Debt approach because no one has demonstrated, or even attempted to show, a viable technique for segregating and separating intangibles.

APPLICABLE LAW

1. The Utah Constitution mandates that all tangible property in the state shall be taxed at a uniform and equal rate. Utah Const. Article XIII, Section 2(1) provides as follows:

So that each person and corporation pays a tax in proportion to the fair market value of his, her, or its tangible property, all tangible property in the state that is not exempt under the laws of the United States or under this Constitution shall be:

- (a) assessed at a uniform and equal rate in proportion to its fair market value, to be ascertained as provided by law; and
- (b) taxed at a uniform and equal rate.

2. Consistent with the Constitutional provisions to tax all property at its fair market value, the Legislature enacted Utah Code Ann. § 59-2-103 (2005), which provides as follows:

(1) All tangible property shall be assessed and taxed at a uniform and equal rate on the basis of its fair market value, as valued on January 1, unless otherwise provided by law.

3. Utah Code Ann. § 59-2-102(12) (2005) defines “fair market value” in relevant part, as follows:

(9) “Fair market value” means the amount at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of the relevant facts. . . .

4. The Legislature has also created by statute an exemption for intangible property. Utah Code Ann. § 59-2-1101 (3)(g) provides as follows:

(3) The following property is exempt from taxation . . . (g) intangible property.

5. In Utah Code Ann. § 59-2-102(19), the Legislature has defined intangible property as

follows:

“Intangible property” means:

- (a) property that is capable of private ownership separate from tangible property, including:
 - (i) monies;
 - (ii) credits;
 - (iii) bonds;
 - (iv) stocks;
 - (v) representative property;
 - (vi) franchises;
 - (vii) licenses;
 - (viii) trade names;
 - (ix) copyrights; and
 - (x) patents. . . .
- (c) goodwill.

- 6. The Commission has adopted Rule 62 for the valuation of state assessed properties.

The relevant portions of that Utah Admin. Rule R884-24P-62 are:

D. General Valuation Principles. Unitary properties shall be assessed at fair market value based on generally accepted appraisal theory as provided under this rule.

* * *

2. The preferred methods to determine fair market value are the cost approach and a yield capitalization income indicator as set forth in E.

a) Other generally accepted appraisal methods may also be used when it can be demonstrated that such methods are necessary to more accurately estimate fair market value.

b) Direct capitalization and the stock and debt method typically capture the value of intangible property at higher levels than other methods. To the extent intangible property cannot be identified and removed, relatively less weight shall be given to such methods in the reconciliation process, as set forth in E.4.

c) Preferred valuation methods as set forth in this rule are, unless otherwise stated, rebuttable presumptions, established for purposes of consistency in mass appraisal. Any party challenging a preferred valuation method must demonstrate, by a preponderance of evidence, that the proposed alternative establishes a more accurate estimate of fair market value.

E. Appraisal Methodologies.

* * *

2. Income Capitalization Approach. Under the principle of anticipation, benefits from income in the future may be capitalized into an estimate

of present value.

a) Yield Capitalization. The yield capitalization formula is $CF/(k-g)$, where "CF" is a single year's normalized cash flow, "k" is the nominal, risk adjusted discount or yield rate, and "g" is the expected growth rate of the cash flow.

(1) Cash flow is restricted to the operating property in existence on the lien date, together with any replacements intended to maintain, but not expand or modify, existing capacity or function. Cash flow is calculated as net operating income (NOI) plus non-cash charges (e.g., depreciation and deferred income taxes), less capital expenditures and additions to working capital necessary to achieve the expected growth "g". Information necessary for the Division to calculate the cash flow shall be summarized and submitted to the Division by March 1 on a form provided by the Division.

* * *

(b) Capital expenditures should include only those necessary to replace or maintain existing plant and should not include any expenditure intended primarily for expansion or productivity and capacity enhancements.

* * *

(3) The growth rate "g" is the expected future growth of the cash flow attributable to assets in place on the lien date, and any future replacement assets.

* * *

F. Property Specific Considerations. Because of unique characteristics of properties and industries, modifications or alternatives to the general value indicators may be required for specific industries.

DISCUSSION

On August 28, 2007, the Commission issued a Findings of Fact, Conclusion of Law, and Final Decision in Appeal Nos. 06-0768 & 06-0740, which has been previously referred to herein as the Prior Airline Decision. In that decision the Commission concluded, based on the evidence and arguments that the parties presented in that matter, that the value should be raised from the APG Wholesale value to APG Retail. The Commission's decision in the subject appeal, although it may appear contradictory to the Prior Airline Decision, is a result of the evidence and testimony submitted in this matter, which was dissimilar to that submitted in the prior appeal.

One key difference between the prior appeal and the subject appeal was that in the prior appeal all parties were arguing for an APG indicator, the dispute being limited to whether the proper indicator was APG Retail or APG Wholesale. In the subject appeal, there was significant testimony that the APG was not a unitary valuation method and that it was not an appropriate appraisal method to determine the unitary value of an operating airline without considering other unitary approaches, further testing,

benchmarking and some independent verification of the data. The testimony supported a conclusion that the corrected income indicator was a viable unitary method and one of the preferred appraisal methods pursuant to Rule 62 for determining the value of PETITIONER. Clearly the evidence failed to demonstrate by a preponderance that the APG established a more accurate estimate of fair market value, as would be required by Utah Admin. Rule R884-24P-62D2(c).

It is clear to the Commission from WITNESS B's testimony that the APG, regardless of which classification is used, cannot be used directly to value any single aircraft in PETITIONER's fleet, or any other fleet for that matter, nor can the APG establish the value of a group of aircraft or a total fleet. WITNESS B's testimony was clear that the APG itself was not an appraisal, that it would not be used as the sole basis for conducting an appraisal, that it was instead one of the data points.⁶¹ The APG, as the testimony shows, may however, be employed as a reference or data point in establishing an actual value.⁶²

Another concern for the Commission in using the APG to estimate fair market value comes from the 2004 COMPANY B Appraisal.⁶³ The appraisal had been prepared at the request of the Division to determine a value for PETITIONER's fleet for the tax year 2004, and was not submitted as an estimate of value for purposes of this proceeding. This appraisal is informative, however, in that it offers an insight and perspective on the relevance of the APG to fair market value and for unitary appraisal purposes. To begin, the report contains no reference to 'fair market value.' Instead the appraisal used the undefined term 'market value.'⁶⁴

Of specific concern to the Commission, nonetheless, is that the 2004 COMPANY B Appraisal states that it is a "valuation opinion for each aircraft," and the individual values were summed for the 'total market value' for the PETITIONER Fleet.⁶⁵ Because of the way that COMPANY B describes its

⁶¹ Findings of Fact 33.

⁶² The Commission has recognized and approved the use of guidebooks similar to the APG in other mass appraisal contexts. Rule 884-24P-47, for example, values aircraft according to prices established in the Aircraft Bluebook Price Digest. Rule 884-24P-33, which contains the Commission's personal property schedules, specifically allows an appraiser to rely on "recognized publications" to approximate the cost of new and used vehicles and specifically lists the Marshall and Swift Cost Index and the Penton Price Digest. These sources are generally recognized as authoritative in determining costs and values and are typically relied on by experts, even though the data used in compiling the guides is proprietary and not generally available to litigants.

⁶³ Petitioner's Exhibit 41.

⁶⁴ Petitioner's Exhibit 41, pg 4.

⁶⁵ Petitioner's Exhibit 41, pg. 4.

appraisal, and that the Division followed the COMPANY B process in preparing its Revised Appraisal, the Commission concludes that the Division has not appraised the fleet component of its APG Market Indicator of Value according to the statutory requirement of fair market value.

The Commission would prefer unitary valuation indicators prepared and considered in the determination of the assessed value of all airlines to reliance solely on an APG indicator. If an airline has no positive income, the APG could be considered as a benchmark along with other unitary approaches. In the complete absence of another meaningful or reliable approach, the Commission may consider the use of the APG as a proxy. However, the Commission notes that given the current market condition of the airline industry as a whole, the APG Wholesale indicator is nearer in value to the Commission's conclusion for the relatively profitable PETITIONER than the APG Retail indicator proposed by the Division.

CONCLUSIONS OF LAW

1. When a taxpayer protests its property tax assessment, the Division “must present available evidence supporting the original valuation” and “once that is done the taxpayer . . . must meet its twofold burden of demonstrating “substantial error or impropriety in the [original] assessment;” and providing “a sound evidentiary basis upon which the Commission could adopt a lower valuation.” (X) v. Utah State Tax Comm'n, 2000 UT 49 ¶ 10, 5 P.3d 652, 655, 656, quoting, (X) v. Tax Comm'n, 590 P.2d 332 (Utah 1979). As a general rule, the “original valuation is entitled to a ‘presumption of correctness.’” Id. at ¶ 9. In the present matter, all parties argued for a value other than the original assessment. The Division made substantial changes to the Original Assessment including a major change in methodology, which resulted in an increased value in the Revised Assessment. The Revised Assessment does not enjoy the presumption of correctness given to the Original Assessment.

2. In the Original Assessment, the Division had determined that the system value was \$\$\$\$\$. It was the Original Assessment that enjoys the presumption of correctness. The Division has a burden in this matter to support raising the value based on the Revised Appraisal. Further, as the Revised Appraisal is based solely on APG Retail, the Commission concludes that the Division has an additional burden under Utah Admin. Rule R884-24P-62, because the APG Retail method is not one of the preferred methods set out in the rule. Rule 62 (4)(iii) states, “any party challenging a preferred valuation method must demonstrate, by a preponderance of evidence, that the proposed alternative establishes a more accurate estimate of fair market value.” The Division failed to establish that the APG Retail

method was a generally accepted appraisal method for the unitary valuation of operating airlines. Although the APG may be recognized as a starting point to determine a value for an airplane or airplanes, it was not a generally accepted appraisal method for determining the unitary value of an operating airline. Additionally, the evidence presented at the hearing did not show that the APG Retail method would more accurately estimate fair market value for the unitary operating airline. The Division did not meet its burden to increase the value of the property to its Revised Appraisal value.

3. During the hearing, the County filed a Motion for Directed Verdict arguing that PETITIONER failed to meet its burden of proof to show error or impropriety in the original assessment or provide a sound evidentiary basis upon which the Commission could adopt a lower value. The Counties point out that PETITIONER submitted no appraisal and had no “expert testimony” to offer a value in this matter. The only witness to offer a conclusion on the value of PETITIONER for the lien date was WITNESS A, PETITIONER’s Director of Property Tax. The County pointed out that she was not an appraiser or appraisal expert but was offered as a fact witness. They also point out that she is not the owner of the subject property. It was WITNESS A who calculated the value that PETITIONER requested for the property. The Commission will consider a property owner’s statement as to the value of the property. Where the property owner is a business, the Commission will allow a representative to speak on the behalf of the business. The weight that the Commission gives the value opinion from the owner or owner’s representative will be based on the qualifications of the witness and facts and circumstances of the appeal. The Commission concludes that PETITIONER did show error in the Division’s complete reliance on the APG indicator, but failed to provide a sound evidentiary basis to support the lower value that it requested.

4. The Commission notes in relation to the County’s Motion for Directed Verdict, the Division also had a burden in this matter. There was a burden on the part of the Division to establish the value above that set in the Original Assessment, and secondarily to establish why the APG should be used to value the property instead of one of the preferred methods listed in Rule 62. Ultimately, after weighing the evidence submitted, including the testimony of WITNESS A, WITNESS C, APPRAISER B and WITNESS B, the Commission concludes it was sufficient to establish error in the Division’s placing 100% of its weight on an APG indicator and that the better valuation method was the yield capitalization income indicator.

Appeal No. 06-0725

FINAL DECISION

Based on the foregoing, the Commission finds that for the lien date January 1, 2006, the Utah assessed value after adjustment for TEFRA of the subject property is \$\$\$\$\$. It is so ordered.

DATED this ____ day of _____, 2009.

Jane Phan
Administrative Law Judge

BY ORDER OF THE COMMISSION:

The Commission has reviewed this decision and the following concur.

DATED this ____ day of _____, 2009.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

D'Arcy Dixon Pignanelli
Commissioner

Marc B. Johnson
Commissioner

NOTICE: You have twenty (20) days after the date of this order to file a Request for Redetermination with the Commission pursuant to Utah Code Ann. § 63G-4-302. A Request for Redetermination must allege newly discovered evidence or a mistake of law or fact. If you do not file a Request for Redetermination with the Commission, this order constitutes final agency action. You have thirty (30) days after the date of this order to pursue judicial review of this order in accordance with Utah Code Ann. § 59-1-601 et seq. and 63G-4-401 et seq.

Appeal No. 06-0725

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