

THE STATE OF SOUTH CAROLINA
IN THE COURT OF APPEALS
APPEAL FROM THE ADMINISTRATIVE LAW COURT

John D. McLeod, Administrative Law Judge

Case No. 11-ALJ-17-0299-CC

Tilbros, Inc.,Respondent,

vs.

Cherokee County Assessor's Office.....Appellant.

INITIAL BRIEF OF APPELLANT

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TABLE OF CONTENTS

Table of Authorities.....	ii
Statement of Issues on Appeal.....	1
I. Whether the Administrative Law Court erred in its valuation of the subject property.....	1
Statement of the Case.....	1
Statement of the Facts.....	2
Argument:	
I. The Administrative Law Judge was incorrect in finding the fair market value of the subject property to be One Million Thirty Two Thousand and No/100 (1,032,000.00) Dollars rather than the value of One Million Eight Hundred Seventy Six and No/100 (\$1,876,000.00) Dollars placed upon the property by the taxing authority.....	4
Conclusion.....	15

TABLE OF AUTHORITIES

CASES

<i>Beverly Hosp. v. South Carolina State Health and Human Servs. Fin. Com'in</i> , 319 S.C. 225, 229, 460 S.E. 2d 383, 385-386 (1995).....	5
<i>CFRE, LLC v. Greenville Cnty. Assessor</i> , 395 S.C. 67, 73, 716 S.E. 2d 877, 880 (2011)...	6
<i>Cloyd v. Mabry</i> , 295 S.C. 86, 376 S.E. 2d 171 (Ct. App. 1988).....	6
<i>Grayson v. Carter Rhoad Furniture</i> , 317 S.C. 306, 309, 454 S.E. 2d 320, 321 (1995).....	6
<i>Mayfair Mills, Inc.</i> , 295 B.R. 827 (U.S. Bankruptcy Court, D., S.C. 2002).....	6
<i>Newberry Mills v. Dawkins</i> , 259 S.C. 7, 190 S.E. 503 (1972).....	6
<i>Original Blue Ribbon Tax Corp. v. S.C. Dep't of Motor Vehicles</i> , 380 S.C. 600, 604, 670 S.E. 2d 674, 676 (Ct. App. 2008).....	6
<i>Smith v. Newberry County Assessor</i> , 350 S.C. 572, 567 S.E. 2d 501 (Ct. App. 2002)....	6, 14
<i>South Carolina Tax Commission v. South Carolina Tax Board of Review</i> , 278 S.C. 556, 299 S.E. 2d 489 (1983).....	6
<i>Taylor v. Aiken County Assessor</i> , 4023 S.C. 559, 741 S.E. 2d 31 (Ct. App. 2013).....	6

STATUTES

S.C. Code Ann. Section 1-23-610(B).....	5
S.C. Code Ann. Section 12-37-930.....	6, 9
S.C. Code Ann. Section 12-37-3140.....	7, 9, 10
S.C. Code Ann. Section 12-43-217.....	7
S.C. Code Ann. Section 12-37-670(B).....	8
S.C. Code Ann. Section 12-37-3140(B).....	8
S.C. Code Ann. Section 12-37-3140(A)(2).....	9
S.C. Code Ann. Section 12-37-3110 et. seq.....	7, 8

Statement of Issues on Appeal

- I. **Whether the Administrative Law Court erred in its valuation of the subject property?**

STATEMENT OF THE CASE

On May 6, 2008 Tilbros, Inc. acquired the real property subject to this appeal for the sales price of Three Million and No/100 (\$3,000,000.00) Dollars. (Petitioner's Exhibit 5 p. 20). The property consists of a three (3) story sixty (60) room hotel on 1.27 acres fronting I-85 in Cherokee County, South Carolina. For the tax year 2010 Cherokee County assessed the value of the real property at One Million Nine Hundred Sixty-Two Thousand Five Hundred and No/100 (\$1,962,540.00) Dollars. Tilbros, Inc. filed a written notice of objection by letter dated September 29, 2010. By letter dated December 14, 2010 Cherokee County reduced the assessed value to One Million Eight Hundred Seventy-Six Thousand and No/100 (\$1,876,000.00) Dollars. Tilbros, Inc. timely filed an appeal with the Cherokee County Board of Assessment Appeals by letter dated January 13, 2011. The Cherokee County Board of Assessment Appeals held a hearing on Tilbros appeal on May 5, 2011. The Board of Assessment Appeals affirmed the County's valuation in its final decision dated May 9, 2011. On June 3, 2011 Tilbros timely filed a notice of and request for a contested case hearing before the S.C. Administrative Law Court. (Petitioner's Exhibit 1, Stipulation of Facts paragraphs 3, 4, 5, 6, 7, 9, 10, 11, 12, 13 and 14).

A contested hearing was held before the South Carolina Administrative Law Court on June 25, 2013. At the hearing the parties stipulated that the valuation date would be December 31, 2008 (Tr. p. 10 ll. 10 – 16; p. 18 ll. 15 – 17 p. 20 ll. 11 - 15). The Honorable John D. McLeod, Administrative Law Judge (ALJ) issued a Final Order and Decision on

October 14, 2013 with said decision being filed on the same date. Cherokee County timely filed and served a Motion to Alter or Amend the judgment dated October 22, 2013. By Order dated November 5, 2013 and filed on the same date the Motion to Alter or Amend was denied. Thereafter, on December 2, 2013 Cherokee County timely filed and served its Notice of Appeal and this appeal follows.

STATEMENT OF THE FACTS

This case is a real property tax appeal. The subject property is a three (3) story sixty (60) bed hotel located off the frontage road of I-85 in Cherokee County. The central issue is the value of the property and improvements as of December 31, 2008. The valuation date was stipulated by the parties and is, therefore, not in dispute. The tax year in dispute is 2010. (Petitioner's Exhibit 1, Stipulation of Facts paragraphs 15 and 16).

On May 6, 2008 Tilbros, Inc. (Respondent herein) purchased the hotel for Three Million and No/100 (\$3,000,000.00) Dollars. (Petitioner's Exhibit 5 Page 20). The Three Million and No/100 (\$3,000,000.00) Dollar figure was the amount listed on the deed. There was some dispute as to whether the Three Million and No/100 (\$3,000,000.00) Dollar figure included only the land and building, or did it also include the value of furniture, fixtures and equipment? No testimony was offered by Tilbros, Inc concerning the breakdown of the purchase price but the appraiser for Tilbros, Inc., Joseph Rosen, testified that the consideration set forth in the deed should only include the land and building and not the furniture, fixtures and equipment. (Tr. p. 77 l. 20 – p. 78 l. 10; p. 105 ll. 15 – 23; p. 106 ll. 4 – 8). However, Mr. Rosen discounted the purchase price by Thirty Eight Thousand and No/100 (\$38,000.00) Dollars, which was the value of the furniture, fixtures and equipment filed in the Cherokee County Auditor's Office. (Tr. p. 106 ll. 17 – 23). The appraiser never got any

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breakdown of values from Tilbros. (Tr. p. 107 I. 23 – p. 108 I. 3; p. 109 I. 19 – p. 110 I. 4). Therefore, according to Tilbros' own expert, the value of the land and building at the time of purchase, May 6, 2008, would be Two Million Nine Hundred Sixty Two Thousand and No/100 (\$2,962,000.00) Dollars. Nevertheless, the appraiser for Tilbros valued the property at Six Hundred Ninety-Eight Thousand and No/100 (\$698,000.00) Dollars as of the valuation date of December 31, 2008, less than eight (8) months later.

When the property was purchased for Three Million and No/100 (\$3,000,000.00) Dollars by Tilbros it lost its flag. It had been a Holiday Inn Express. The term flag represents the branding of the hotel. (Tr. p. 28 II. 22 – 25). The hotel operated with no flag from May 6, 2008 until August 30, 2008 (Tr. p. 33 I. 21 – p. 34 I. 8; p. 35 I. 2 – p. 36 I. 10; p. 37 II. 8 – 13). At that time the hotel was converted to a Sleep Inn and has been operated as such through the date of the hearing in this matter. (Tr. p. 37 II. 14 – 25). Also, according to Mr. Rosen the hotel had an occupancy rate of 96 percent when it was acquired by Tilbros but the occupancy rate dropped to 35½ percent by December 2008. (Tr. p. 36 II. 11 – 22).

Although, Mr. Rosen recognized there are three (3) different methods of valuation; namely, the cost approach, the sales comparison approach and the income approach, he only used the income approach (Tr. p. 72 II. 4 – 10). Mr. Rosen rejected the other two (2) approaches completely (Tr. p. 72 II. 11 – 24; p. 74 II. 8 – 10; p. 74 I. 23 – p. 76 I. 21).

Cherokee County presented the expert testimony of its tax assessor, Robert Weaver. Mr. Weaver is licensed as an appraiser in both North Carolina and South Carolina. Unlike the appraiser hired by Tilbros, Mr. Weaver used two (2) different approaches to come to the value of the real property in question. Mr. Weaver used both the income approach and the

cost approach. (Tr. p. 174 ll. 11 – 15, Respondent Exhibit 6). Using the cost approach Mr. Weaver opined the value of the subject property to be One Million Eight Hundred Seventy-Six and No/100 (\$1,876,000.00) Dollars. (Tr. p. 174 l. 16 – p. 175 l. 2). Using the income approach Mr. Weaver opined the value of the subject property to be Two Million One Hundred Forty Two Thousand and No/100 (\$2,142,000.00) Dollars. (Tr. p. 178 l. 2 – p. 181 l. 4). However, at the appeal board level Mr. Weaver recommended the lesser figure of One Million Eight Hundred Seventy Six Thousand and No/100 (\$1,876,000.00) Dollars. (Tr. p. 181 l. 19 – p. 182 l. 2). Even after the appeal board ruling Mr. Weaver continued to look at additional data to assist him in valuing the subject property. Based on the additional data Mr. Weaver revised his income approach value to One Million Nine Hundred Seventeen Thousand and No/100 (\$1,917,000.00) Dollars. (Tr. p. 182 l. 3 – p. 183 l. 7).

Therefore, in the final analysis, this case presents an opinion from the expert hired by the taxpayer that the subject property has a value of Six Hundred Ninety Eight Thousand and No/100 (\$698,000.00) Dollars utilizing only one (1) method of valuation. And the expert testimony of the Cherokee County Tax Assessor that the subject property has a value of One Million Eight Hundred Seventy Six and No/100 (\$1,876,000.00) Dollars utilizing two (2) different methods of valuation, with the assessor taking the lesser value of the two (2) different approaches.

ARGUMENT

The Administrative Law Judge was incorrect in finding the fair market value of the subject property to be One Million Thirty Two Thousand and No/100 (\$1,032,000.00) Dollars rather than the value of One Million Eight Hundred Seventy Six and No/100 (1,876,000.00) Dollars placed upon the property by the taxing authority.

A. STANDARD OF REVIEW

The Administrative Procedures Act establishes the Court's standard of review for cases decided by the ALC and is set forth in Section 1-23-610(B) of the South Carolina Code (Supp. 2009), which provides:

The review of the administrative law judge's order must be confined to the record. The court may not substitute its judgment for the judgment of the administrative law judge as to the weight of the evidence on questions of fact. The court of appeals may affirm the decision or remand the case for further proceedings; or, it may reverse or modify the decision if the substantive rights of the petitioner have been prejudiced because the finding, conclusion, or decision is:

- a) in violation of constitutional or statutory provisions;
- b) in excess of the statutory authority of the agency;
- c) made upon unlawful procedure;
- d) affected by other error of law;
- e) clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record; or
- f) arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion.

The appellate court must affirm an administrative agency's decision if the decision is supported by substantial evidence and the appellate court may not substitute its judgment for that of the agency upon questions for which there is room for difference of intelligent opinion. *Beverly Hosp. v. South Carolina State Health & Humans Servs. Fin. Com'in*, 319 S.C. 225, 229, 460 S.E. 2d 383, 385-386 (1995). "Substantial evidence is not a mere scintilla of evidence, but evidence which, considering the record as a whole would allow reasonable minds to reach the conclusion the agency reached," *Grayson v. Carter Rhoad*

Furniture, 317 S.C. 306, 309, 454 S.E. 2d 320, 321 (1995). Cited by *Smith v. Newberry County Assessor*, 350 S.C. 572, 567 S.E. 2d 501 (Ct. App. 2002).

“Tax appeals to the ALC are subject to the Administrative Procedures Act.” *CFRE, LLC v. Greenville Cnty. Assessor*, 395 S.C. 67, 73, 716 S.E. 2d 877, 880 (2011). “The decision of the [ALC] should not be overturned unless it is unsupported by substantial evidence or controlled by some error of law.” *Original Blue Ribbon Taxi Corp. v. S.C. Dep’t of Motor Vehicles*, 380 S.C. 600, 604, 670 S.E. 2d 674, 676 (Ct. App. 2008). Questions of statutory interpretation are questions of law, which the appellate court is free to decide without any deference to the court below. Cited by *Taylor v. Aiken County Assessor*, 402 S.C. 559, 741 S.E. 2d 31 (Ct. App. 2013).

B. PRESUMPTION OF CORRECTNESS

It has long been held that the assessor’s assessment of value carries a presumption of correctness and cannot be set aside unless the property owner proves the actual value of the property. *Cloyd v. Mabry*, 295 S.C. 86, 376 S.E. 2d 171 (Ct. App. 1988), citing *Newberry Mills v. Dawkins*, 259 S.C. 7, 190 S.E. 2d 503 (1972) and *South Carolina Tax Commission v. South Carolina Tax Board of Review*, 278 S.C. 556, 299 S.E. 2d 489 (1983). This presumption has never been abolished and remains the law of this state. *In Re: Mayfair Mills, Inc.*, 295 B.R. 827 (U.S. Bankruptcy Court, D. S.C. 2002). This presumption was cited by the Administrative Law Judge in his Order. (Final Order p. 7 paragraph 10). However, for the reasons set forth below, appellant would assert the ALJ failed to properly apply this presumption.

C. STATUTORY CONSTRUCTION

Pursuant to S.C. Code Ann., Section 12-37-930 “All property must be valued for

taxation at its true value in money which in all cases is the price which the property would bring following reasonable exposure to the market, where both the seller and the buyer are willing, are not acting under compulsion, and are reasonably well informed of the uses and purposes for which it is adapted and for which it is capable of being used..." The above code section must be read and construed in conjunction with the South Carolina Real Property Valuation Reform Act, S.C. Code Ann. Sections 12-37-3110 et. seq.. The applicable of section 12-37-3140 in effect at the time of valuation reads as follows:

- A)(1) For property tax years beginning after 2006, the fair market value of real property is its fair market value applicable for the later of:
 - a) the base year, as defined in subsection (C) of this section;
 - b) December thirty-first of the year in which an assessable transfer of interest has occurred;
 - c) as determined on appeal; or
 - d) as it may be adjusted as determined in a countrywide reassessment program conducted pursuant to Section 12-43-217, but limited to increases in such value as provided in subsection (B) of this section.
- (2) To the fair market value of real property as determined at the time provided in item (1) of this subsection, there must be added the fair market value of subsequent improvements and additions to the property.
- B) Any increase in the fair market value of real property attributable to the periodic countywide appraisal and equalization program implemented pursuant to Section 12-43-217 is limited to 15 percent within a five (5) year

period to the otherwise applicable fair market value. However, this limit does not apply to the fair market value of additions or improvements to real property in the year those additions or improvements are first subject to property tax, nor do they apply to the fair market value of real property when an assessable transfer of interest occurred in the year that the transfer value is first subject to tax.

- C) for purposes of determining a "base year" fair market value pursuant to this section, the fair market value of real property, is its appraised value applicable for property tax year 2007;
- D) Real property valued by the unit valuation concepts is excluded from the limits provided pursuant to subsection (B) of this section.
- E) Values attributable to additions and improvements and changes in value resulting from assessable transfers of interest occurring in a property tax year are first subject to property tax in the following tax year except as provided pursuant to Section 12-37-670(B).

It is important for the court to appreciate the interplay between these two (2) statutes. The appellant would assert that the ALJ did not apply both of these statutes to the valuation process therefore the ALJ committed an error of law which should be corrected by this Honorable Court.

In 2007 the S.C. Real Property Valuation Reform Act (S.C. Code Ann. 12-37-3110 et. seq.) became effective. Section 12-37-3140 (B) places a cap of 15 percent to any increase in value every five (5) years based on solely on an increase in value and not a sale,

change of use or additional improvements. Because of this cap, the initial assessment of the value of property is very important. If a property is grossly undervalued at the initial assessment the taxing authority cannot adjust the value more than 15 percent every five (5) years thus creating a potential windfall for the taxpayer. Recognizing this potential problem the legislation included Section 12-37-3140(A)(2) which reads, "To the fair market value of real property as determined at the time provided in item (1) of this subsection, there must be added the fair market value of subsequent improvements and additions to the property."

In the present case Tilbros, Inc. purchased a hotel which at the time of purchase had lost its flag. Tilbros, made upgrades to the property and eventually obtained the Sleep Inn flag. The valuation date was December 31, 2008 which was shortly after the hotel began operating under the Sleep Inn flag. Also, as the appraiser goes to great lengths to point out, this is right after the banking crisis of the fall of 2008. As set forth below the appraisal of Tilbros, Inc is fatally flawed. The ALJ failed to properly construe the S.C. Code Ann. Sections 12-37-930 and 12-37-3140 and should have reviewed the valuations in light of these statutes.

In the present case when Tilbros purchased the property they lost the flag (branding) of the property. As Tilbros appraiser points out this includes the loss of the reservation system of the branded hotel. Therefore, the hotel must "recover" from this loss. In the present case Tilbros rebranded the hotel as a Sleep Inn and began operating under this flag on August 30, 2008. As pointed out by both appraisers, hotels are unique for assessment purposes. Hotels are income producing and, therefore, the income approach is one of the methods of calculating value. Although Tilbros' "improvements" to the property did not come after December 31, 2008, the true effects of the improvements would not be felt until after December 31, 2008. The appraiser for Tilbros wants to take a "snapshot" of value

isolated to December 31, 2008 whereas the tax assessor includes information beyond December 31, 2008 for similar income producing hotels so that a true value can be derived.

The approach of the tax assessor is in conformity with Section 12-37-3140 and the approach by Tilbros' appraiser is not. Surely any reasonable person or investor realizes that it takes a reasonable amount of time to see the benefits from the improvements. Here the Tilbros appraiser bases the occupancy rate and the expense rate on an "effective" five (5) months. In reality here's what happened. Prior to the purchase of the hotel it had a 96 percent occupancy rate. Tilbros purchases the hotel for Three Million and No/100 (\$3,000,000.00) Dollars on May 6, 2008, the hotel then loses its flag and reservation system. Tilbros makes improvements and on August 30, 2008 the hotel is re-branded as a Sleep Inn. The four (4) months of time from August 30, 2008 until December 31, 2008 is just insufficient upon which to base a value under the income approach because the impact of the improvements will not be truly seen until later. That's why the tax assessor included data from other sources when calculating the occupancy rate, the average daily rate and the expense ratio. What the tax assessor did was in conformity with Section 12-37-3140 and what the appraiser for Tilbros did was not in conformity with the statute.

Therefore, the ALJ committed an error of law in utilizing an appraisal method that did not comply with the law.

D. ABUSE OF DISCRETION.

S.C. law does not require the use of any particular method of valuing property. Both experts in this case recognize there are generally three (3) different methods to determine the value of real property. The cost approach, the sales comparison approach and the income approach (Tr. p. 72 ll. 4 – 10). The appraiser for Tilbros only used the income

approach and did not use the cost approach or the sales comparison approach. (Tr. p.; 72 l. 11 – 24; p. 74 l. 8 – p. 76 l. 21). In using the income approach Tilbros appraiser utilized the “Rushmore” method which he candidly characterized as the most conservative approach as opposed to other methods such as the Total Assets of Business approach. (Tr. p. 41 l. 12 – p. 42 l. 21). In his appraisal the appraiser for Tilbros recognizes that the value of the subject property is fluid and not static. The report states “constantly changing economic, social, potential and physical conditions have varying effects upon real property values. Even after the passage of a relatively short period of time, property values may change substantially and require a review based on differing market conditions”. (Petitioner’s Exhibit 5 pp. 10 and 11). The report also notes that the subject property had a 2008 assessed value of Two Million Two Hundred Thirty Three Thousand Six Hundred and No/100 (\$2,233,600.00) Dollars; that the property was purchased for Three Million and No/100 (\$3,000,000.00) Dollars on May 6, 2008; that it operated with no flag for almost four (4) months in 2008 but on August 30, 2008 the hotel opened as a Sleep Inn; and that the hotel had good site data including good visibility from I-85. (Petitioner’s Exhibit 5, pp. 14, 20, 21 and 23). However, the appraiser concludes that because of the economic downtime as of December 31, 2008 the value of the hotel had plummeted to Six Hundred Ninety Eight Thousand and No/100 (\$698,000.00) Dollars. The appraisal mentions the cost approach but only to the extent that the appraiser didn’t use the approach for various reasons. However, oddly, the appraisal has a section dealing with the Sales Comparison Approach. In this section the appraiser cites five (5) hotels which sold near the time of the subject property. These sales range from a high Five Million Two Hundred Thousand and No/100 (\$5,200,000.00) Dollars to a low of Two Million and No/100 (\$2,000,000.00) Dollars. Interestingly the hotel in Wilson, North Carolina sold for Two Million

One Hundred Fifty Thousand and No/100 (\$2,150,000.00) Dollars on December 1, 2008 after the economic downturn relied upon by the appraiser. After citing these comparable sales the appraiser simply dismissed the information as being unreliable. This utter dismissal of the sales comparison approach is contrary to the advice offered by Daniel H. Lesser in the article submitted by Tilbros (Petitioner's Exhibit 9). On page 14 of the article the author states ... "the sales comparison approach may provide a range of values to bracket and support the final estimate of value..." In the present case, the appraiser should not have dismissed his own comparables but he should have heeded the advice contained in the article he submitted. The five (5) comparables have an average sales price of Two Million Six Hundred Thirty Five Thousand Four Hundred and No/100 (\$2,635,400.00) Dollars. This figure certainly gives credence to the market value placed upon the property by the tax assessor and contradicts the value placed on the property by the appraiser for Tilbros. However, Tilbros' appraiser used the data from these same five (5) sales hotels to support his finding of a 12 percent capitalization rate for the subject property when utilizing the income approach for determining value. The appraiser never explains why these five (5) comparables are reliable as far as obtaining a capitalization rate, yet not reliable for sales comparisons. This is important since the higher the capitalization rate the lower the value of the subject property. Also, in that same article the writer suggests the first thing to do if a property owner suspects his property is incorrectly valued is to look at other similar properties in the tax jurisdiction (Petitioner's Exhibit 9 page 25). The tax assessor did this analysis (Respondent's Exhibit 10). The tax assessor listed six (6) other hotels in Cherokee County, while Tilbros did not. A review of these other hotel values leads to the inescapable conclusion that the correct value of the subject property is the value placed upon the property by the tax assessor and not the appraiser for Tilbros.

However, the biggest flaw in Tilbros' appraisal comes from the figures the appraiser uses for the occupancy rate and the expense ratio. According to Tilbros appraiser the occupancy rate of the hotel was 96 percent when purchased by Tilbros in May 2008. The hotel immediately lost its flag and operated with no flag until August 30, 2008. In his appraisal the Tilbros appraiser comes up with an occupancy rate of 35.5 percent based upon four (4) months of actual data. (September through December 2008). He also comes up with an expense rate of 73 percent using this same data. While it is true the ALJ does not have to accept the opinion of an expert in toto, there should be some rational basis to accept the expert's report. The ALJ clearly believed the expense rate of 73 percent to be in error since the ALJ reduced it to 66 percent in the Final Order. In fact, the 73 percent ratio had no support in fact. This lack of rational bases is exposed in the appraisal for Tilbros (Petitioner's Exhibit 5 page 71). The appraiser for Tilbros uses actual data from the operation of the hotel. The appraiser calls it an "effective" five (5) months of data. He uses the term "effective" because from May 6, 2008 until August 30, 2008 Tilbros operated the hotel without a flag while they made improvements so they could obtain the Sleep Inn flag. Even assuming this data to be accurate, the hotel had an expense ratio of 62.31 percent. This 62.31 percent ratio is set forth in the Chart on page 71 of Petitioner's Exhibit 5. On page 72 of the same exhibit the appraiser for Tilbros declares the actual expense ratio to be 62.31 percent. The appraiser declares "after analyzing subject's effective five (5) months of income and expense in 2008, the NOI (Net Operating Income) is 37.7 percent and the expense ratio is 62.31 percent. Yet without a calculation or explanation the appraiser "adjusts" the expense ratio to 73 percent. While the ALJ was correct in rejecting the expense ratio, it was an abuse of discretion for the ALJ to "re-write" the appraisal for Tilbros and come up with a 66 percent expense ratio. After the ALJ

found such a glaring error in the appraisal the ALJ should have rejected the appraisal as not reflecting the true value of the hotel and upheld the value placed upon the property by the taxing authority was required by law.

In summary, to accept the value opined by Tilbros the finder of fact would have to accept the following propositions. The value of hotel on May 6, 2008 was at least Two Million Nine Hundred Sixty Two Thousand and No/100 (\$2,962,000.00) Dollars. This represents the purchase price of Three Million and No/100 (\$3,000,000.00) Dollars less Thirty Eight Thousand and No/100 (\$38,000.00) Dollars for the value of the furniture, fixtures and equipment. While the purchase price of the property is evidence of value, it is not conclusive. *Smith v. Newberry County Assessor*, 350 S.C. 572, 567 S.E. 2d 501 (Ct. App. 2002). That the hotel lost its flag and operated as an unbranded hotel from May 6, 2008 until August 30, 2008. During this time there is no data for occupancy rates. That the new owners upgraded the property and obtained the Sleep Inn flag on August 30, 2008. That four (4) months of true income and expense data coming off a four (4) month period of transition was a correct indicator of value to be used in the income approach to determine fair market value. That no other approach to determine value is reliable in the present situation. That the value of the property plummeted to Six Hundred Ninety Eight Thousand and No/100 (\$698,000.00) Dollars in eight (8) months. The appellant would assert that it was an abuse of discretion for the ALJ to use the opinion of Tilbros' expert in determining value.

Also, appellant would assert that the law requires the ALJ to use the value of the taxing authority unless Tilbros provides the true value. The ALJ rejected the value of Six Hundred Ninety Eight Thousand and No/100 (\$698,000.00) Dollars asserted by Tilbros. Therefore, Tilbros did not prove true value. Under the law the value of the taxing authority

would therefore prevail.

CONCLUSION

The appellant would assert that this Honorable Court should reverse the final order of the Administrative Law Court and find the value of the subject property to be One Million Eight Hundred Seventy Six and No/100 (\$1,876,000.00) Dollars.



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April 28, 2014.

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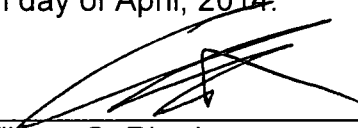
Cherokee County Assessor's Office.....Appellant.

PROOF OF SERVICE

I, William G. Rhoden, Esquire, Counsel for Respondent in the above referenced matter, certify that I have served the within **Initial Brief of Appellant and Appellant's Designation of Matter to be Included in the Record on Appeal** by depositing a copy of same in the United States Mail, postage prepaid, addressed as follows:

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Dated this 28th day of April, 2014.



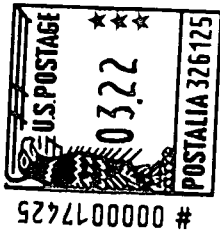
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