

Rosebrook Water Co., Inc.

v.

Town of Carroll

Docket No.: 19382-01PT

DECISION

The “Taxpayer” appeals, pursuant to RSA 76:16-a, the “Town’s” 2001 assessment of \$412,300 on Map 999/Lot UTL/Sublot WAT, a water utility infrastructure consisting primarily of water mains located in the Town (the “Property”). For the reasons stated below, the appeal for abatement is denied.

The Taxpayer has the burden of showing, by a preponderance of the evidence, the assessment was disproportionately high or unlawful, resulting in the Taxpayer paying a disproportionate share of taxes. See RSA 76:16-a; TAX 201.27(f); TAX 203.09(a); Appeal of City of Nashua, 138 N.H. 261, 265 (1994). To establish disproportionality, the Taxpayer must show the Property’s assessment was higher than the general level of assessment in the municipality. Id. We find the Taxpayer failed to prove disproportionality.

The Taxpayer argued the assessment was excessive because:

(1) the Property was purchased for \$250,000 in late 1999 through an arm’s-length stock transaction;

(2) the rates charged by the Taxpayer for providing water are regulated by the New Hampshire Public Utilities Commission (“PUC”) which limits the Taxpayer to a 10% rate of return and does not allow a management expense;

(3) a reasonable allocation of the total property owned by the Taxpayer is 65% within the Town and 35% within the Town of Bethlehem; and

(4) using an income approach and applying the 65% allocation factor yields a market value of the Property of approximately \$146,400, well below the assessed value.

The Town argued the assessment was proper because:

(1) historically, utilities are assessed based upon the cost approach, less applicable depreciation;

(2) the Town previously believed there were 13,693 feet of water mains, but in actuality there were 36,671 feet in the Town based on PUC information;

(3) the allocation of property between Carroll and Bethlehem, based on replacement cost, should be approximately 69% and 31%, not materially different than the Taxpayer’s allocation of 65% and 35%;

(4) using a depreciated cost approach based on Marshall and Swift replacement cost estimates and applying appropriate physical, functional and economic depreciation, the valuation of the actual 36,671 feet of water main is \$449,078.70;

(5) an income approach estimate, based on an estimate of a maximum net operating income of \$54,000 and an overall capitalization rate of 8.34%, indicates an allocated market value for the Carroll property of approximately \$420,000;

(6) the guaranteed rate of return as allowed by the PUC indicates there is relatively little risk in this investment;

(7) the Taxpayer's opinion of value is from a representative who is not a licensed appraiser and who has no experience valuing utility property; and

(8) the Taxpayer failed to sustain its burden of proof.

Board's Rulings

Based on the evidence, the board finds the Taxpayer failed to prove the assessment was disproportionate.

The Property under appeal consists of various-sized water mains and meters for a system that supplies water to approximately 300 commercial and residential properties in the Town, including the Mount Washington Hotel. The water supply (wells, pumps and tank) is located in the adjoining town of Bethlehem. The Taxpayer is a public utility regulated by the PUC which has oversight in the determination of water rates and the maximum rate of return on the net book value of the Property's assets.

The Town based its assessment of \$412,300 on an estimated total lineal footage of the various-sized water mains of 13,540 feet. As presented by the Town at hearing and as supported by Municipality Exhibit A (the Annual Report of the Rosebrook Water Company, Inc. to the PUC ("Annual PUC Report")), the actual amount of water mains located in Carroll is approximately 36,671 lineal feet or almost three times the estimate on which the assessment was based.

There are three generally-recognized approaches to value: 1) the cost approach; 2) the comparables sales approach; and 3) the income approach. Appraisal Institute, The Appraisal of Real Estate 62 (12th Ed. 2001). With respect to public utilities, the supreme court has expanded on these basic appraisal approaches, as noted in Public Serv. Co. v. Town of Ashland, 117 N.H. 635, 638 (1977):

“There are five approaches to valuation potentially applicable to utility property: original cost less depreciation; reproduction cost less depreciation; comparable sales; capitalized earnings; and the cost of alternative facilities capable of delivering equivalent energy. New England Power Co. v. Littleton, 114 N.H. at 598, 326 A.2d at 701. All the approaches are valid, but all also have weaknesses.”

The parties focused their arguments on the income (capitalized earnings) and cost approaches mentioned in Public Service, *supra*.

The Taxpayer’s representative, Mr. Mark Lutter argued the income approach to value was the most applicable approach for valuing a small water company, such as the Taxpayer’s, because its income and expenses are easily determined from the public filings with the PUC and the PUC restricts the rate of return on investment. Mr. Lutter estimates a market value for the entire water system in both towns of approximately \$225,225 and allocates 65% to the Town to arrive at an estimated market value of \$146,400.

Secondarily, Mr. Lutter argued the 1999 stock transfer from a Mr. Satter to the Mount Washington Hotel Preservation Limited Partnership (“MWH”) for \$250,000 was an arm’s-length transaction and, thus, a further consistent indication of market value.

The Town primarily submitted a replacement cost less depreciation approach based on the actual footage of water mains and meters within the Town and applying physical depreciation to the water mains at 2.25% per year (based on an assumption of all being installed in 1974) with additional depreciation of 5% functional and 10% economic for outdated technology, PUC regulation and the relatively small size of the customer base. The Town’s estimated market value by this approach was \$449,079 (rounded).

The Town also estimated a value by the income approach, modifying Mr. Lutter's numbers and capitalization rate to arrive at an estimated market value of \$420,000.

The board finds that either the cost or income approaches are applicable for a water utility of this size that has an identifiable physical plant for which estimated depreciation can be calculated and which has income and expense information that is readily available through the Annual PUC Report.

First, however, we find Mr. Lutter's income approach calculations are flawed and understate the Property's value. Mr. Lutter's assumption that a \$29,000 management and owner salary should be deducted from the maximum potential income of approximately \$54,000 (derived by the maximum 10% return on the Property's net book value as shown on page 14 of Municipality Exhibit A) is not supported by the evidence contained both in the Annual PUC Report and in the Town's testimony that such costs are not deducted from the maximum potential income but rather are passed through as administrative expenses, as long as they are reasonable and included in the water rates. Further, the board finds the Town's testimony and evidence relative to applicable mortgage and equity rates more reasonable and market related than Mr. Lutter's. The Town testified its mortgage rates were derived from discussions with a commercial loan officer in Concord that such commercial rates are based on the federal home loan rate as opposed to the prime rate used by Mr. Lutter. In addition, the board finds Mr. Lutter's use of a 15% equity rate for this type of property is excessive due to the guaranteed rate of return at 10% allowed by the PUC. Utilizing the Town's lower mortgage and equity rates and not deducting the management salary results in an overall market value of approximately

\$647,500 which, when allocated based on the parties' allocation estimate of 65% for the Town, results in an indicated market value of \$420,000.

Second, the board finds the replacement cost new less depreciation approach is also an appropriate approach to value the Property. Again, the length and size of the water mains and their ages are all public information and reasonable replacement cost estimates can be derived from cost manuals such as the one published by Marshall and Swift Valuation Service. Specifically, the board finds the Town's replacement cost estimates and depreciation submitted at hearing are reasonable and are supported by the documents and other evidence. If anything, the Town's estimates are conservative since it assumed all installation of the water mains occurred at the initial installation date (1974), while the evidence indicates that some water mains have been added somewhat later. Further, the Town's rate of physical depreciation of 2.25% is similar to the depreciation charges of 2.0% for the water mains and 2.02% rate overall for all facilities the Taxpayer reported on page 24 of the Annual PUC Report.

The board disagrees with Mr. Lutter's argument (contained in the appeal document) that the 1999 stock transfer of \$250,000 is some indication of market value for several reasons. First, there was no evidence that the Property had been or would likely be openly marketed in the traditional manner of real estate. The fact it was a stock transfer and that the Property is a water utility with a discrete customer base indicates that it is unlikely the Property was or could be openly marketed. Also, there was testimony that Mr. Satter had previously had an interest in MWH and related development in the Bretton Woods area and for unknown reasons was transferring the Property after his interests in those other properties had been transferred. Further, MWH, the purchaser of

the stock, is the Taxpayer's largest customer (purchasing nearly 75% of the Taxpayer's water in 2000 – see page 41 of the Annual PUC Report) and, thus, had significant motivation to acquire the Property to ensure continued viability of the water utility. In short, the transaction has a number of factors that makes it suspect as an arm's-length transaction and, thus, we have given it little weight. Society Hill at Merrimack Condo. Assoc. v. Town of Merrimack, 139 N.H. 253, 255-56 (1994).

Mr. Lutter also argued that the water meters were not taxable as real estate and, therefore, should be omitted from the assessment. First, this is a de minimis argument as the water meters comprise slightly more than 2% of the assessed value and less than 1% of the estimated market value submitted at hearing by the Town in its replacement cost less depreciation value estimate. Regardless, however, of the magnitude of the meters' assessed value, the board finds that the meters are an integral part of the Taxpayer's physical plant and are taxable as real estate. As the Town testified based on its experience with assessing water companies throughout the state and indeed with the Taxpayer itself, the trend is towards metering all water sold to customers for accuracy and billing documentation. Water meters for measuring the deliverance of water to customers is similar to pumps at gas stations which are an integral party of the system delivering gasoline and are taxable as real estate. Cf. Haselton v. Town of Derry, BTLA Docket No. 16932-96PT (January 15, 1999), 1999 WL 147845; VSH Realty Inc. v. Town of Tilton, Docket No. 16224-95PT (March 20, 1997), 1997 WL 159439, and Haselton v. Town of Derry, Docket No. 14962-93PT (December 20, 1996), 1996 WL 861946.

Last, arriving at the conclusion that the Taxpayer failed in its burden and the Town submitted adequate documentary evidence to support its assessment (albeit, based

on the wrong lineal footage of water mains), is acknowledgement both of the fact that Mr. Lutter has had no experience in valuing or representing public utilities (as he testified, this is the first appeal in which he represented a utility) and of the Town's representative's many years of assessing varying types of utilities throughout the state and his knowledge of the applicable valuation approaches to such utilities.

Finally, as noted during the hearing, the board has a concern with Mr. Lutter, an experienced tax consultant, significantly modifying and adding to the grounds for appeal stated in the appeal document between the time of filing the appeal and the date of hearing. Such modifications and expansion of the grounds for appeal are prohibited by TAX 203.03(g), which states: "Throughout the appeal, the issues raised by the Taxpayer in the Abatement Application and Appeal Document may differ, but the grounds stated in the Appeal Document shall control the issues before the Board." In this case, the Town graciously waived objecting to Mr. Lutter's subsequently-developed income approach argument, and thus the board allowed Mr. Lutter to present such evidence. However, Mr. Lutter should be aware of this rule in the future in other appeals and ensure that he represents his clients properly by adequately and fully stating at the time of filing all grounds on which the appeal is based.

A motion for rehearing, reconsideration or clarification (collectively "rehearing motion") of this decision must be filed within thirty (30) days of the clerk's date below, not the date this decision is received. RSA 541:3; TAX 201.37. The rehearing motion must state with specificity all of the reasons supporting the request. RSA 541:4; TAX 201.37(b). A rehearing motion is granted only if the moving party establishes: 1) the decision needs clarification; or 2) based on the evidence and arguments submitted to the board, the board's decision was erroneous in fact or

in law. Thus, new evidence and new arguments are only allowed in very limited circumstances as stated in board rule TAX 201.37(f). Filing a rehearing motion is a prerequisite for appealing to the supreme court, and the grounds on appeal are limited to those stated in the rehearing motion. RSA 541:6. Generally, if the board denies the rehearing motion, an appeal to the supreme court must be filed within thirty (30) days of the date on the board's denial.

SO ORDERED.

BOARD OF TAX AND LAND APPEALS

Paul B. Franklin, Chairman

Albert F. Shamash, Esq., Member

Certification

I hereby certify a copy of the foregoing Decision has this date been mailed, postage prepaid, to: Mark Lutter, representative for the Taxpayer, Northeast Property Tax Consultants, 37 Crystal Avenue – PMB 290, Derry, New Hampshire 03038; Gary Roberge, representative for the Town, Avitar Associates of New England, Inc., Post Office Box 981, Epsom, New Hampshire 03234; and Chairman, Board of Selectmen of Carroll, Post Office Box 146, Twin Mountain, New Hampshire 03595.

Date: March 24, 2004

Anne M. Stelmach, Deputy Clerk