BEFORE THE IDAHO BOARD OF TAX APPEALS

L&S INVESTMENTS OF IDAHO #5, LP, Appellant, v. KOOTENAI COUNTY, Respondent.	)	APPEAL NO. 21-A-1029 FINAL DECISION AND ORDER

COMMERCIAL PROPERTY APPEAL

This appeal is taken from a decision of the Kootenai County Board of Equalization denying an appeal of the valuation for taxing purposes on property described by Parcel No. S300000L009A. The appeal concerns the 2021 tax year.

This matter came on for telephonic hearing October 26, 2021, before Board Member Leland Heinrich. Member David Pace appeared at hearing for Appellant. Kootenai County Assessor Bela Kovacs represented Respondent.

Board Members Leland Heinrich, David Kinghorn, and Kenneth Nuhn join in issuing this decision.

The issue on appeal concerns the market value of an improved commercial property.

The decision of the Kootenai County Board of Equalization is affirmed.

FINDINGS OF FACT

The assessed land value is $117,312, and the improvements' value is $934,489, totaling $1,051,801. Appellant agrees with the land value, but contends the correct value of the improvements is $328,159, for a total valuation of $445,471.

The subject property is a .65 acre commercial parcel located in Spirit Lake, Idaho. The property is improved with two (2) low-income multifamily apartment buildings. All the units in the apartment complex have one (1) bathroom, though they vary in bedroom count. Specifically, the subject complex is comprised of four (4) one (1) bedroom units, two (2) two (2) bedroom units, and six (6) three (3) bedroom units. The subject property has been used solely to provide low-income housing to qualified applicants since 1983, and is so restricted until the expiration of the loan agreement with the Rural Development and Rural Housing Service under the United States Department of Agriculture, which is scheduled to expire in April 2034.

Appellant disagreed with the valuation methodology Respondent used to assess the subject property. Specifically, Appellant objected to Respondent's use of market rents and expenses in its income approach model, which in Appellant's view inflated the net operating income and reduced expenses, thereby resulting in a higher net operating income figure. As a Section 42 development project, Appellant argued subject's actual income and expenses should be used as provided in Idaho Code § 63-205A.

Respondent agreed Idaho Code requires Section 42 low-income projects to be specially assessed using the specific development's actual income and expenses. However, Respondent highlighted Idaho Code § 63-205A(2)(d) which requires an owner of a Section 42 low-income housing development to annually provide the facility's financial statements to the Idaho State Tax Commission (STC) by April 1 of the relevant year, otherwise the property is to be assessed using market rents and expenses. In this case, Appellant did not provide subject's financial statements to the STC by the statutory deadline, so Respondent assessed the property using market income and expenses.

Appellant acknowledged subject's financial statements were not timely filed with the STC but maintained subject's current valuation was still too high. Appellant pointed to a portion of the definition of market value provided in Idaho Code § 63-201(15). In particular, Appellant focused on the term "informed, capable buyer" and argued an informed buyer would recognize subject is a low-income housing development and would base a purchase decision on the facility's actual financial performance, not the market rates non-restricted apartment complexes are able to achieve in the marketplace. Appellant pointed to Idaho Code § 63-208(1), which mandates a property's "actual and functional use be a major consideration" in determining market value for assessment purposes. Linking this passage with "informed, capable buyer," Appellant reasoned subject's actual financial statements should be used to develop an income approach valuation model, because subject is actually and functionally used as a Section 42 property, and a potential buyer would factor the restricted use and lower income associated with such a property in a decision to purchase the property. Using subject's audited three (3) year stabilized financial statements and a capitalization rate of 8.2% in its income approach model, Appellant concluded a market value of $445,471 for the property.

Respondent maintained because subject's financial statements were not timely filed with the STC, the property must be assessed at market value. Therefore, Respondent developed value estimates using all three (3) recognized appraisal approaches. The cost approach yielded a value indication of $973,177, though details were somewhat limited.

While not a traditional sales comparison approach model wherein recent sales of similar type property are compared to subject and appraisal adjustments are made for differences in property characteristics, Respondent did offer some raw sales data in support of subject's current valuation. The data set included four (4) apartment complex sales from 2019 and one (1) from 2020. The sale properties were constructed between 1963 and 1995 and concerned apartment complexes with unit counts ranging from five (5) to twenty (20) units. Sale prices ranged from $444,596 to $1,648,744, or an average of $110.80 per square foot. Subject's improvements were assessed at $86.51 per square foot, which Respondent noted was less than the average range indicated by the sales data.

Lastly, Respondent provided details concerning its income approach model, which was ultimately used to set subject's current assessed value. Respondent explained it had recently completed a rent study of apartments throughout the county in an effort to identify market rental rates. Focusing on apartment complexes constructed prior to 1987, Respondent reported an average monthly rental rate of $746 for a one (1) bedroom, one (1) bathroom apartment, and an average rate of $955 for two (2) bedroom, one (1) bathroom units. Respondent did not have rental data for three (3) bedroom units in older apartment complexes. In valuing the subject property, Respondent's income model used monthly rental rates of $720 and $790 for subject's one (1) and two (2) bedroom units, respectively, and $930 per month for subject's three (3) bedroom units. A vacancy rate of 3% was applied, as was a market expense rate of 28%, resulting in a net operating income figure of roughly $84,000. The net operating income was capitalized at 8%, which rate was loaded with the 1.17% local tax levy. Respondent concluded a value of $934,489 for the improvements, which, after adding the land value of $117,312, yielded a total value of $1,051,801, which is subject's current assessed value.

CONCLUSIONS OF LAW

This Board's goal in its hearings is the acquisition of sufficient, accurate evidence to support a determination of market value in fee simple interest, or, as applicable, a property's exempt status. This Board, giving full opportunity for all arguments and having considered all the testimony and documentary evidence submitted by the parties, hereby enters the following.

The primary issue is whether the subject property qualifies for the special valuation treatment for assessment purposes as a Section 42 low-income property pursuant to Idaho Code § 63-205A. For the reasons below, the Board finds subject does not qualify for special valuation treatment for 2021.

Absent an express exemption, all property within Idaho is subject to appraisal, assessment, and property taxation. Idaho Code § 63-203. While not an "exemption" in the traditional sense, Section 42 provides low-income housing developments are eligible for special valuation treatment for purposes of assessment under Idaho Code § 63-205A, which provides in pertinent part,

> (2) The market value for assessment purposes of section 42 low-income properties shall be determined by the county assessor using the following criteria:
>
> > (a) The sales comparison approach using similar rent restricted properties, the cost approach, and the income approach, shall be considered in valuing section 42 low-income properties . . . The three (3) approaches will be reconciled into a single property value.
> >
> > . . .

> The net operating income shall be capitalized into value using a market derived capitalization rate. To determine the net operating income, effective gross income shall be reduced by costs customary to section 42 operations, including normalized operating expenses plus all compliance, audit, asset management and other fees . . .
>
> > (d) Beginning in 2010, the owners of properties described in this section *shall provide to the Idaho state tax commission no later than April 1 of each year*, such financial statements from the prior year as are customarily prepared in the ownership and operation of any section 42 property . . . If such information is not made available to the Idaho state tax commission and county assessors, each county *shall substitute market rent apartment derived expenses and income* for section 42 low-income properties.
> >
> > (Emphasis added).

As the above code section makes clear, in order to utilize a facility's actual income and expense data, the owner of a Section 42 property *must* provide financial statements annually to the Idaho State Tax Commission (STC) by April 1; April 1, 2021, in the instant appeal. Failure to provide such financial information results in the property being assessed as a non-rent-restricted apartment complex using market income and expenses. Appellant admittedly did not provide subject's financial statements to the STC by the deadline; therefore, the property does not qualify for special valuation treatment under Idaho Code § 63-205A.

As the Idaho Supreme Court held in *Corp. of the Presiding Bishop of Church of Jesus Christ of Latter-Day Saints v. Ada Cnty.*,

> Idaho case law requires that all tax exemption statutes be strictly and narrowly construed against the taxpayer, who must show a clear entitlement, and in favor of the state. Courts may not presume exemptions, nor may they extend an exemption by judicial construction where not specifically authorized. The language of exemption statutes must be given its ordinary meaning and an exemption will not be sustained unless within the spirit as well as the letter of the law.
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> 123 Idaho 410, 416, 849 P.2d 83, 86 (1993).

"It should further be observed that a grant of exemption from taxation is never presumed and statutes and constitutional provisions relating to exemptions should be strictly construed, and where a doubt arises it should be resolved against the exemption." *Lewiston Orchards Irrigation Dist. v. Gilmore*, 53 Idaho 377, 383, 23 P.2d 720, 722 (1933). Applied here, the relevant statute required Appellant to provide subject's financial statements to the STC by April 1, 2021, and where that did not occur, the Board must deny Appellant's claim for special valuation treatment for the subject property as outlined by the controlling statute.

Having determined subject does not satisfy the requirements of Idaho Code § 63-205A, the issue now concerns the accuracy of subject's current market value assessment.

Idaho Code § 63-205 requires taxable property be assessed at market value annually on January 1; January 1, 2020, in this case. Market value is always estimated as of a precise point in time. Idaho Code § 63-201 provides the following definition,

> "Market value" means the amount of United States dollars or equivalent for which, in all probability, a property would exchange hands between a willing seller, under no compulsion to sell, and an informed, capable buyer, with a reasonable time allowed to consummate the sale, substantiated by a reasonable down or full cash payment.

Market value is estimated according to recognized appraisal methods and techniques. The sales comparison approach, the cost approach, and the income approach comprise the three (3) primary methods for determining the market value of real property. *Merris v. Ada Cnty.*, 100 Idaho 59, 63, 593 P.2d 394, 398 (1979). The income approach is commonly used in the valuation of commercial properties, as the income-producing potential of a commercial property is often a primary consideration in a prospective buyer's purchasing decision.

Appellant argued the above market value definition would still require subject's actual income and expenses be used to value the property because "an informed, capable buyer" would place emphasis on subject's restricted use and income in deciding whether to purchase the property. While the Board concurs that Idaho generally requires a property's actual and functional use to be a major consideration in that property's valuation, such is not the case here. Subject is a Section 42 low-income housing development, which is a distinct property type for which Idaho has developed a special assessment procedure.

As discussed earlier, the actual normalized income and expense data is to be used when assessing a Section 42 property, provided the STC is given the facility's financial statements by April 1. When financial statements are not provided, Idaho Code § 63-205A(2)(d) requires the assessor to "substitute market rent apartment derived expenses and income for section 42 low-income properties." So, while a potential purchaser of a low-income property would likely be willing to pay less than what they would for an otherwise similar non-restricted apartment complex, the controlling statute effectively imposes the extraordinary hypothetical condition that the property is not rent-restricted. The statute directs the assessor to value the property as an unrestricted apartment complex, which naturally requires use of market-derived inputs into the income approach model.

Though Respondent developed value opinions using all three (3) approaches to value as required by the statute, ultimately the income approach formed the basis for subject's current assessment. The Board finds no error in Respondent's emphasis on the income approach, because subject is an income-producing property, and the approach is commonly relied on by market participants. It was also not lost on the Board the rent figures used in Respondent's valuation model were lower than the average rental amounts indicated by Respondent's rent study, resulting in a relatively conservative valuation.

Idaho Code § 63-511 places the burden on the Appellant to demonstrate error in subject's valuation by a preponderance of the evidence. Given the record in this matter, the Board did not find the burden of proof satisfied. The subject property did not qualify for the special valuation treatment afforded by Idaho Code § 63-205A and therefore must be assessed using market-derived income and expenses, which is precisely how the property was assessed. Appellant did not offer competing market-based evidence to counter the information offered by Respondent, nor did the evidence otherwise suggest an adjustment is warranted in this instance. In all, the Board found subject's current assessed value adequately supported in the record.

Based on the above, the decision of the Kootenai County Board of Equalization is affirmed.

FINAL ORDER

In accordance with the foregoing Final Decision, IT IS ORDERED that the decision of the Kootenai County Board of Equalization concerning the subject parcel be, and the same hereby is, AFFIRMED.

DATED this 4th day of January, 2022.