BEFORE THE IDAHO BOARD OF TAX APPEALS

RILEY HILL, Appellant, v. PAYETTE COUNTY, Respondent.	)	APPEAL NOS. 21-A-1091, 21-A-1092, and 21-A-1093 FINAL DECISION AND ORDER

COMMERCIAL PROPERTY APPEALS

These appeals are taken from three (3) decisions of the Payette County Board of Equalization modifying appeals of the valuation for taxing purposes on properties described by Parcel Nos. F3600005001A, F3600005001B, and F3600005001C. The appeals concern the 2021 tax year.

These matters came on for telephonic hearing December, 15, 2021, before Hearing Officer Travis VanLith. David Pace appeared at hearing for Appellant. Payette County Assessor Edie Aldridge represented Respondent.

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

The issues on appeal concern the market values of three (3) improved commercial properties.

The decisions of the Payette County Board of Equalization are affirmed.

FINDINGS OF FACT

Parcel No. F3600005001A (Appeal 21-A-1091)

The assessed land value is $56,875, and the improvements' value is $615,254, totaling $672,129. Appellant agrees with the land value, but contends the correct value of the improvements is $203,192, totaling $260,067.

Parcel No. F3600005001B (Appeal 21-A-1092)

The assessed land value is $45,500, and the improvements' value is $362,901, totaling $408,401. Appellant agrees with the land value, but contends the correct value of the improvements is $113,588, totaling $159,088

Parcel No. F3600005001C (Appeal 21-A-1093)

The assessed land value is $25,100, and the improvements' value is $131,875, totaling $156,975. Appellant agrees with the land value, but contends the correct value of the improvements is $37,438, totaling $62,538.

The subject properties are three (3) contiguous parcels totaling 2.07 acres in size and operated collectively as a low-income housing development in Fruitland, Idaho. There are a total of thirty-six (36) units spread across eight (8) two-story buildings with a combined 30,620 square feet of finished living area. The apartment complex was constructed in three (3) phases from 1984 to 1988. As the subject properties are operated as part of a common enterprise, they will be referred to as a single property for purposes of this decision

The subject property was partially developed in 1988 through tax credits received under the Section 42 low-income housing program. The tax credits have since expired, but the property is currently financed, in part, under Section 515 of the National Housing Act. As a Section 515 project, subject operates strictly to provide affordable housing to applicants satisfying certain income criteria. The land use restrictions imposed on the subject property by the government run with the land and will continue to be in force until the expiration of the loan agreement, scheduled to end in 2038, roughly seventeen (17) years from now. In Appellant's view, subject's restricted rents and constrained land use were inadequately considered in the current assessed value.

As subject is an affordable housing development and will be for the foreseeable future, Appellant advocated the income approach as the most reliable valuation methodology for determining the property's current market value. Calculated using subject's trailing three (3) years financial statements, Appellant input subject's stabilized income and expense numbers in the valuation model, which yielded a stabilized net operating figure of roughly $40,000. Appellant started with a 6.8% market-extracted capitalization rate sourced from a reputable national publication, to which an effective property tax rate of 1.32% was added, as well as a .26% risk adjustment factor, equating to an overall capitalization rate of 8.38%. The result was a final value indication of $481,693 for the subject property, which Appellant allocated between the subject parcels according to their relative contribution to the total assessed value of the development.

Respondent noted subject was once a Section 42 housing development, but the status was lost some years ago. It was explained once a property loses its Section 42 status, it ceases to be considered a low-income housing project for assessment purposes, and the property is assessed at market value. With respect to subject being a Section 515 housing development, Respondent pointed out that while subject's rents are restricted, the property receives subsidies from various government sources to close the gap between the restricted rental rates and market rent. So, in effect, the property is operating with market-level revenues, which is why Respondent assesses such properties consistent with non-restricted housing developments.

Similar to Appellant, Respondent developed a direct capitalization income model in support of subject's current assessed value. Respondent utilized subject's actual 2020 revenues as the effective gross income for its model but used normalized market expenses in calculating subject's net operating income at approximately $100,000. The net operating income was capitalized at 4.64%, which was extracted from sales data included in Respondent's sales comparison analysis below. The result was a total value indication of $2,198,030, or $61,056 per unit for the subject housing complex.

Respondent's sales model included twelve (12) sales which transpired between February 2020 and April 2021. Two (2) of the sales concerned tri-plex properties constructed in 1903 and 1905, both of which have been updated. The data set also included seven (7) four-plex properties constructed in 2020. And the remaining three (3) sale properties were a six (6) unit complex, an eleven (11) unit development, and a sixteen (16) unit project, constructed in 1937, 1993, and 1987. Overall sale prices ranged from $155,000 to $1,350,000, or from $46,000 to $135,000 per unit. Respondent concluded a total value of $2,279,821 for the subject development from this analysis.

Respondent additionally prepared a market-correlated cost approach analysis. This model yielded a value of $1,379,821 for subject's improvements. Three (3) vacant land sales were used to develop an opinion of subject's land value. Sale No. 1 concerned a 1.23 acre vacant parcel which sold in October 2020 for $117,110, or $95,211 per acre. Sale No. 2 was a .35 acre lot with a reported February 2020 sale price of $59,900, or

$171,143 per acre. Sale No. 3[1] was also a .35 acre parcel, which sold for $78,000, or $222,857 per acre, in October 2020. Respondent determined a value of $900,000, or $434,783 per acre, for subject's 2.07 acres. In sum, Respondent petitioned subject's assessed value be increased to $2,279,821, with $1,379,821 attributable to the improvements and $900,000 to the land.

CONCLUSIONS OF LAW

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

Idaho Code § 63-205 requires taxable property be assessed at market value annually on January 1; January 1, 2021, in this case. Market value is always estimated as of a precise point in time. Market value is defined in Idaho Code § 63-201, as,

> "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 three (3) primary approaches for determining market value include the sales comparison approach, the cost approach, and the income approach. *Merris v. Ada Cnty.*, 100 Idaho 59, 63, 593 P.2d 394, 398 (1979). The market value of commercial

1 It appears Sale Nos. 2 and 3 are the same property. Respondent did not comment on any of the vacant land sales; however, the sales grid reflects two (2) parcel numbers connected with Sale No. 2, but only one (1) of those same parcel numbers was indicated for Sale No. 3. Respondent reported identical lot sizes of .35 acres for both sales, so it is likely the two (2) parcels included in Sale No. 2 were combined into the single parcel involved in Sale No. 3.

property can be estimated using all three (3) approaches, though the income approach is commonly utilized, because commercial property is often traded in the marketplace based on its income-producing potential.

Appellant developed an income approach model using subject's stabilized revenues and expenses over the prior three (3) years. The net operating income was capitalized at 8.38%, which yielded a total value indication of $481,693. Respondent questioned the roughly 80% expense ratio reflected in Appellant's model and stated a more typical expense rate for subject's property type is closer to 50%. Respondent also disagreed with the 8.38% capitalization rate utilized by Appellant. A representative from the Idaho State Tax Commission who regularly oversees valuations of low-income housing properties reported current local capitalization rates range from 5.5% to 6%. Appellant was willing to accept the lower market capitalization rate but maintained the local tax levy rate should be added, as well as a risk factor for subject being a rent-restricted property.

Important in determining a reliable estimate of market value using the income approach is the use of market-level revenues and expenses, not necessarily the actual financial figures of the particular property being valued. Using market rates is particularly critical in the context of assessment, which constitutionally requires uniform taxation across the same class of properties. Use of market rates reduces the potential influence management decisions may have on the performance of any specific business. A unique commercial property type may require use of the actual revenue and expense data, because there is not enough information in the marketplace to ascertain market rates. In the case of the subject property, the Board took no issue with Appellant's use of subject's stabilized revenues, because the subsidies the property receives through the Section 515 program are intended to bring the revenues up to market, and thus subject is realizing revenues at market levels.

The Board was concerned, however, with the expenses reported by Appellant, which equated to a roughly 80% expense ratio. Most of the expenses were ordinary in the Board's view, but others appeared somewhat high. For example, the reported management fees were nearly 15% of the effective gross income. In the Board's experience, management expense fees are more commonly in the 5% range. The Board was also not convinced the 8.38% capitalization rate used in Appellant's model was appropriate, particularly the addition of a .26% risk adjustment, for which Appellant offered no market-based support. In short, the Board had too many concerns to rely solely on Appellant's income model in determining subject's current market value.

Respondent offered value opinions using all three (3) valuation approaches, which efforts were appreciated by the Board. Respondent's cost approach model estimated a value of $1,379,821 for subject's improvements and $900,000 for the land. Respondent did not provide much discussion of its cost approach, but the Board found several of the inputs into the model somewhat curious. According to the ProVal summary sheets, 0% physical deprecation was applied to subject's improvements, despite them being constructed in the mid-1980s. Typically, the Board would expect to see some depreciation for roughly thirty-five (35) year old improvements. Nothing in the record suggested subject's improvements had been extensively renovated recently, so the reason for the 0% physical depreciation factor remains unknown.

The Board was similarly concerned with Respondent's $900,000 value conclusion for subject's land. Respondent reported three (3) vacant lot sales, though from the limited information provided it appeared Sale Nos. 2 and 3 concerned the same .35 acre lot which sold in February 2020 for $59,900, and again eight (8) months later for $78,000. Sale No. 1 was a 1.23 acre parcel with an October 2020 sale price of $117,110. On a per-acre basis, Respondent reported price rates from roughly $95,000 to $223,000 per acre. Based on these sales, Respondent concluded a value of $900,000 for subject's 2.07 acres, which equates to approximately $435,000 per acre. On its face, Respondent's proposed land value is dubious, as the per-acre rate is nearly double the highest price rate in the record. This runs contrary to the principle of economies of scale, which in the context of real property, stands for the proposition that a larger parcel commands less value per unit (acre) than an otherwise similar parcel smaller in size. Not only were the sale lots a fraction of subject's size, but none sold anywhere near the $435,000 per acre rate Respondent argued for subject's land value. In short, the Board was reluctant to place much emphasis on Respondent's value conclusion for subject's land.

With respect to Respondent's sales comparison analysis, the Board was again not convinced the value conclusion represented the best indicator of subjects' current market value. Ten (10) of the twelve (12) sales in the data set involved rental properties with six (6)[2] or fewer units, and seven (7) of those properties were four-plexes constructed in 2020. The subject development totals thirty-six (36) units and was constructed in the mid-1980s, which places it in a different class of rental property than triplex and four-plex

[2] Respondent reported Sale No. 3 was a six (6) unit rental property; however, at only 1,452 square feet, it is notably smaller than every other sale property. Presumably, the unit count is actually less than indicated by Respondent, because with a total size figure of 1,452 square feet, each unit would be only 242 square feet in size, which seems unlikely to the Board.

properties, especially those in the data set constructed in 2020, roughly thirty-five (35) years after the subject development was built. The Board understands Respondent was limited to the sales available at the time of assessment, but with such striking differences in physical characteristics between subject and the sale properties, and with no comparative analysis offered by Respondent to adjust for some of those differences, the Board placed minimal emphasis on Respondent's sales grid.

Respondent's income approach model was better received by the Board; however, there were a couple areas of concern. Though Respondent reported subject's 2019 and 2020 actual revenues and vacancies, only the 2020 data was used in the model, which had higher revenues and lower vacancy. Relying on only a single year's income and vacancy data can skew the results if the revenues and vacancies are atypically high or low in the particular year being utilized. Stabilized figures over a couple years are generally considered more reliable information, because the impact of a single atypical year on the value conclusion is minimized by considering multiple years of financial data.

The Board's other primary concern with Respondent's income approach was the 4.64% capitalization rate, which was extracted from an unrestricted apartment sale and represented the lowest capitalization rate of the twelve (12) sales in Respondent's data set by a sizeable margin. The remaining sales varied in capitalization rates from 6.76% to 10.46%, which range is well above the 4.64% rate advocated by Respondent. A representative from the Idaho State Tax Commission reported current market capitalization rates for low-income housing properties in Idaho ranging from 5.5% to 6%. Respondent did not explain why the lower capitalization rate was used in its analysis instead of a rate within the range indicated by the Idaho State Tax Commission representative, but from all the other information provided pointing to higher capitalization rates, Respondent's 4.64% rate appears to be an outlier. Without additional support for the 4.64% capitalization rate, the Board was hesitant to accept the value indication yielded by Respondent's income model.

As market participants typically rely on the income approach for estimating the market value of income-producing property, it is reasonable to use the same approach for valuing the subject development. Due to questions with various aspects of the parties' respective income models, the Board found it necessary in this instance to make some adjustments. Both parties utilized subject's actual revenue and vacancy figures, which were deemed to be at market levels. Appellant used subject's three (3) year stabilized revenues and vacancy, whereas Respondent relied on just 2020 numbers. The Board preferred Appellant's stabilized figures, which provided a better view of subject's operational performance over several years. As discussed earlier, some of the expenses appeared somewhat high to the Board. For this reason, Respondent's operating expense figures were favored, with a small adjustment to the property tax and insurance expense number. Respondent used $36,946 in its analysis, whereas the actual 2020 figure was $38,733.

As for the capitalization rate, the 4.64% rate used by Respondent was an anomaly compared to all the other sales data, which pointed to notably higher capitalization rates. Appellant's capitalization rate was taken from a publication reporting national rates, so was not specific to subject's area. Appellant accepted the 5.5%to 6% range reported by the State Tax Commission representative as likely more reflective of the local marketplace. The Board agrees. Using Appellant's effective gross income and

Respondent's operating expenses, with the small adjustment to the tax and insurance figure noted above, as well as a 6% capitalization rate, calculates to a value of roughly $1,210,000. Capitalizing the same net operating income at 5.5% yields a value indication of approximately $1,320,000. Subject's current assessed value is $1,237,505, which the Board finds reasonable given the indicated value range.

In accordance with Idaho Code § 63-511, Appellant bears the burden of proving 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. In the Board's view, the parties' respective value positions represented opposing outer boundaries of the potential value spectrum, but it is more likely subject's market value lies somewhere between. In the end, subject's current assessed value of $1,237,505 was found to be reasonable considering the information provided in the record.

Based on the above, the decisions of the Payette County Board of Equalization are affirmed.

FINAL ORDER

In accordance with the foregoing Final Decision, IT IS ORDERED that the decisions of the Payette County Board of Equalization concerning the subject parcels be, and the same hereby are, AFFIRMED.

DATED this 12th day of April, 2022.