BEFORE THE IDAHO BOARD OF TAX APPEALS

MELALEUCA, INC., Appellant, v. MADISON COUNTY, Respondent.	)))))))))))	APPEAL NOS. 24-A-1113, 24-A-1114, and 24-A-1115 FINAL DECISION AND ORDER

COMMERCIAL PROPERTY APPEALS

These appeals are taken from decisions of the Madison County Board of Equalization modifying the valuations for taxing purposes on properties described by Parcel Nos. RPRRXB10390140, RPRRXB10390160, and RPRRXB10390200. The appeals concern the 2024 tax year.

These matters came on for hearing November 4, 2024, in Rexburg, Idaho, before Board Member Doug Wallis. Attorney Isaac Eddington appeared at hearing for Appellant. Madison County Assessor Shawn Boice represented Respondent.

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

The issue on appeal concerns the market value of three (3) contiguous commercial properties.

The decisions of the Madison County Board of Equalization are modified.

FINDINGS OF FACT

<u>Parcel No. RPRRXB10390140 (Appeal #24-A-1113)</u>

The original assessed land value was $142,700, and the improvements' valuation was $27,970, totaling $170,670. The Madison County Board of Equalization (BOE) reduced the land value to $93,600, but left the value of the improvements unchanged, for a total valuation of $121,570. For purposes of this decision, this subject parcel will be referred to as Lot 140.

Parcel No. RPRRXB10390160 (Appeal #24-A-1114)

The original assessed land value was $411,950 and the improvements' valuation was $2,341,670, totaling $2,753,620. The BOE reduced the land value to $270,200 and increased the value of the improvements to $2,386,600, totaling $2,656,800. For purposes of this decision, this subject parcel will be referred to as Lot 160.

Parcel No. RPRRXB10390200 (Appeal #24-A-1115)

The original assessed land value was $85,890 and the improvements' valuation was $18,410, totaling $104,300. The BOE reduced the land value to $56,340, but left the value of the improvements unchanged, for a total valuation of $74,750. For purposes of this decision, this subject parcel will be referred to as Lot 200.

Appellant contends the correct combined total value of all three (3) subject parcels is $2,129,194.

The subject properties are three (3) contiguous commercial parcels located in Rexburg, Idaho. The properties collectively[1] serve as a call center, referred to locally as the Melaleuca Call Center. The call center is a 25,952 square foot single level concrete tilt-up building originally constructed in 1973 and 1975 as a Safeway grocery store. The building's primary footprint is on Lot 160 but also extends to Lots 140 and 200. In 2004, the building was converted from retail use to an office call center facility. The interior layout was described as a large open cubicle outlay for most of the space, with individual

[1] The Melaleuca Call Center is comprised of four (4) total parcels, though only three (3) are included in this matter. The fourth parcel is a .38 lot to the front of the building under a different ownership. The combined site totals 2.479 acres in size.

enclosed areas around the periphery comprised of private offices, conference rooms, training rooms, associate lounges, and restrooms. It was noted the only exterior windows are along the old storefront, so natural light is limited throughout much of the interior space.

Appellant disagreed with subjects' original assessments, as well as the reduced values ordered by the BOE, so offered an independent fee appraisal of the subject properties in support of a lower valuation. The appraisal evaluated the three (3) subject parcels and the non-appealed fourth parcel as a single combined call center property. Due to subject's age and attendant physical depreciation, and the functional obsolescence inherent in the building's original design and construction as a retail grocery store, the appraisal contended the cost approach was not the most reliable indicator of subjects' market values.

In estimating the potential gross income for its income model, the appraisal analyzed four (4) lease comparables from the local Rexburg area. With the exception of a building constructed in 1978, the lease comparables were all notably newer than subject, and all were smaller in size, ranging from roughly 3,000 to nearly 11,000 square feet. The appraisal characterized subject's square footage as atypically large for the local office market. Triple net lease rates varied from $7.78 to $25.00 per square foot. After adjustments for location, size, age/condition, and quality/appeal, the appraisal determined adjusted lease rates from $7.00 to $11.25 per square foot. At hearing, the appraiser also shared a $9.00 per square foot lease rate for a call center building with roughly one-half (½) subject's square footage in the immediate neighborhood. Given the lease data, with emphasis on the reported nearby lease rate, the appraisal concluded a lease rate of $8.00 per square foot for the subject call center.

In evaluating an appropriate vacancy and credit loss factor, the appraisal noted vacancy rates in eastern Idaho have been decreasing since the sharp increase in 2020 caused by the pandemic. A commercial brokerage firm reported an average office vacancy rate of 4.1% as of the end of 2023, and a 7.8% rate for multi-tenant office space. National and regional data suggested average vacancy rates of 9.6% and 11.2%, respectively. The appraisal found a 10% vacancy rate appropriate for the subject call center facility.

As the concluded lease rate is a triple net rate, wherein the tenant is responsible for operating expenses, the appraisal noted the landlord's expenses included only management fees and reserves for replacement. It was explained management fees typically vary from 2% to 5%. The appraisal used a 3% management factor and a 2% reserves for replacement factor, resulting in a net operating income figure of roughly $177,000.

For its capitalization rate, the appraisal examined eight (8) sales in Idaho which transpired from September 2020 through December 2023. The sale buildings ranged in size from 2,400 to nearly 44,000 square feet and were constructed between 1992 and 2017. Capitalization rates varied from 6.47% to 7.95%, with an average of 7.24%. The appraisal also cited an investor survey for non-institutional quality properties, which reported capitalization rates from 8.05% to 10.45%, with an average of 9.25%. The appraisal concluded an 8.00% capitalization rate, which, after applied to the net operating income, yielded a value indication of $2,220,000 for the subject call center.

The appraisal next developed a comparative sales model in which five (5) sales were compared to the subject call center, and adjustments were made for differences in key property characteristics. The four (4) sales in Idaho Falls, characterized as a superior location, transpired between April 2020 and July 2023. The sale buildings were constructed from 1988 to 2008 and ranged in leasable area from roughly 8,400 to 11,000 square feet. Sale prices ranged from $1,400,000 to $2,025,000, or from $166.94 to $183.72 per square foot. The lone sale in Rexburg concerned a 7,700 square foot building constructed in 2005, which sold in July 2020 for $580,000, or $75.32 per square foot. After adjustments for location, size, age/condition, quality/appeal, and functional utility, the appraisal determined adjusted sale prices from $61.77 to $100.17 per square foot, with an average rate of $87.03 per square foot. Given the adjusted sale price data, with emphasis on the Rexburg sale, the appraisal concluded a value of roughly $80 per square foot, or $2,080,000, for the subject call center.

In the final reconciliation, the appraisal afforded more weight to the income approach on account of the strength of the rental data gathered and the market-based support for the conclusions reached therein. Also, citing that buyers of subjects' property type mostly purchase for owner-occupancy, the appraisal also gave weight to the sales comparison approach. Ultimately, the appraisal concluded a value of $2,200,000[2] for the subject call center.

In support of subjects' current valuations, Respondent developed value opinions using all three (3) approaches to value. Marshall Valuation Service (MVS) was used to evaluate subject as an average Class C office building constructed in the 1970s. The yard

[2] This $2,200,000 figure represents the value of all four (4) parcels comprising the entire call center property. Subjects' combined pro-rata share of total value conclusion is $2,129,194.

improvements were separately valued. A 45% physical depreciation factor was applied to the building, and a 50% factor to the yard improvements. Respondent applied the lowest land value schedule to subjects' 1.351 acres, resulting in a land value of approximately $270,000. Respondent's cost model concluded a combined value of roughly $2,600,000 for the subject properties, though Respondent acknowledged the cost approach is the least reliable valuation approach in this instance due to the age of subjects' improvements.

Respondent employed the same general methodology in its income approach as used in Appellant's appraisal, though there were some differences in the inputs into its model. Respondent utilized a lease rate of $9.00 per square foot to calculate a potential gross income estimate of nearly $235,000. To this, Respondent applied a 5% vacancy and collection loss factor and a 5% management rate, resulting in a net operating income of roughly $172,000. Applying a 7% capitalization rate yielded a value conclusion of $2,948,000.

Respondent's sales model was comprised of three (3) local sales. Sale No. 1 concerned a 23,444 square foot building constructed in 2014. The first floor was noted to be dedicated to retail use and the upper floor to office. The property sold in February 2022 for $4,200,000. Sale No. 2 was a 14,469 square foot office building constructed in 2005 with an April 2020 purchase price of $1,275,000. Sale No. 3 was a 5,906 square foot building with an unknown age, which sold for $550,000 in October 2019. Respondent applied time adjustments to the respective sale prices using the annual cost change tables published by MVS. This resulted in a roughly 10% increase in the price of Sale No. 1 to $4,628,400, and the 36.5% time adjustment factor applied to Sale Nos. 2 and 3 yielded adjusted prices of $1,740,375 and $750,750, respectively. Based on the adjusted price rates, which varied from roughly $120 to $197 per square foot, Respondent concluded a value of $2,656,800, or $102.37 per square foot for subject.

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.

Idaho Code § 63-205 requires taxable property be assessed at market value annually on January 1; January 1, 2024, 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 market value. *Merris v. Ada Cnty.*, 100 Idaho 59, 63, 593 P.2d 394, 398 (1979). Due its income-producing potential, market participants typically rely on the income approach to estimate the market value of commercial property, though the sales comparison approach is also commonly emphasized.

The Board appreciated the parties' efforts in analyzing subjects' current market values using multiple valuation models. The parties agreed that due primarily to the age of subjects' improvements and the inherent difficulty in accurately estimating depreciation, the cost approach was the least reliable methodology to value the subject properties. As such, the Board sees little benefit in analyzing Respondent's cost model.

Though there were some similarities between the parties' respective income approach analyses, there were also a couple key differences. On an overall basis, the respective income models utilized similar vacancy, management, and reserves for replacement factors. The differences were in the lease rates used to calculate the potential gross income estimates and in the capitalization rates applied to the respective net operating income figures. Respondent offered no support for its $9 per square foot lease rate other than vague references to lease rates involving dissimilar properties. Likewise, the source of Respondent's 7% capitalization rate was unclear. The income model in Appellant's appraisal, on the other hand, offered recent lease and sales data in support of its concluded lease rate of $8 per square foot and an 8% capitalization rate. The subject property was evaluated against the lease and sales comparables, with consideration given to subject's atypically large size in the local office marketplace and the fact the building was originally designed as a grocery store. In all, the Board found the appraisal's income model represented the better supported and more sound income approach analysis.

In similar fashion, the Board found Respondent's sales comparison model represented the less thorough consideration of subjects' current market values. While comprised entirely of local sales, the most recent occurred in early 2022, roughly two (2) years prior to the relevant date of valuation in this matter. With the exception of one (1) sale building, which was also the newest and comprised of retail space on the ground floor, the sale properties were considerably smaller than the subject building.

The Board understands Respondent was constrained to the few number of local sales which have occurred, but it was not apparent how the adjusted sale prices, which ranged from roughly \$120 to \$197 per square foot, correlated to subjects' combined valuation of approximately \$110 per square foot. In short, the Board was not persuaded Respondent's sales comparison analysis yielded the most reliable indication of subjects' current market values.

Idaho Code § 63-511 places the burden on Appellant to establish subjects' valuations are erroneous by a preponderance of the evidence. Given the record in this matter, the Board finds the burden of proof satisfied. Appellant offered an independent appraisal of the subject property, which analyzed the market value of the subject call center using market-supported income and sales comparison valuation models. The Board found Respondent's general methodology reasonable, but support was lacking for some of key variables in its analyses. Accordingly, the Board will modify the decisions of the Madison County Board of Equalization to reflect a combined total value of \$2,129,194 for the subject properties, as detailed below.

FINAL ORDER

In accordance with the foregoing Final Decision, IT IS ORDERED that the decisions of the Madison County Board of Equalization concerning the subject parcels be, and the same hereby are, MODIFIED to reflect the following values:

Parcel No. RPRRXB10390140 (Appeal No. 24-A-1113)

Land:	$69,851
Improvements:	$20,873
Total:	$90,724

Parcel No. RPRRXB10390160 (Appeal No. 24-A-1114)

Land:	$ 201,642
Improvements:	$1,781,045
Total:	$1,982,687

Parcel No. RPRRXB10390200 (Appeal No. 24-A-1115)

Land:	$42,045
Improvements:	$13,738
Total:	$55,783

IT IS FURTHER ORDERED, pursuant to Idaho Code § 63-1305, any taxes which have been paid in excess of those determined to have been due be refunded or applied against other *ad valorem* taxes due from Appellant.

Idaho Code § 63-3813 provides that under certain circumstances the above-ordered value for the current tax year shall not be increased in the subsequent assessment year.

DATED this 20th day of February, 2025.