BEFORE THE IDAHO BOARD OF TAX APPEALS

DDR NAMPA, LLC, Appellant, v. CANYON COUNTY, Respondent.	)	APPEAL NO. 15-A-1101 FINAL DECISION AND ORDER

COMMERCIAL PROPERTY APPEAL

This appeal is taken from a decision of the Canyon County Board of Equalization denying the protest of valuation for taxing purposes of property described by Parcel No. 304980110. The appeal concerns the 2015 tax year.

This matter came on for hearing November 9, 2015 in Caldwell, Idaho before Board Member Leland Heinrich. Attorney Robert Burns appeared at hearing for Appellant. Chief Deputy Assessor Joseph Cox represented Respondent.

Board Members David Kinghorn, Linda Pike and Leland Heinrich participated in this decision.

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

The decision of the Canyon County Board of Equalization is reversed.

FINDINGS OF FACT

The assessed land value is $3,649,890, and the improvements' value is $5,804,000, totaling $9,453,890. Appellant contends the correct total value is $3,130,000.

The subject property is a 12.15 acre parcel located in a multi-parcel retail shopping center in Nampa, Idaho, commonly referred to as the Nampa Gateway Center. The parcel is improved with four (4) large retail buildings constructed in 2007, each capable of housing multiple tenants. Combined, the buildings consist of 160,625 square feet of mostly unfinished leaseable retail space.

Appellant provided a retrospective fee appraisal report with an effective valuation date of January 1, 2015. The appraisal examined the various components of the shopping center and developed value opinions for each. The appraisal outlined the history of the shopping center's development. After purchasing the site in 2005, Appellant spent roughly two (2) years blasting and developing the difficult ground. During this time, development commenced on a new retail shopping center a few miles from subject. The new shopping center was able to attract several large anchor tenants, which helped fuel the demand for smaller retailers and related businesses. By the time the Nampa Gateway Center was ready for tenants, most large anchor tenants were already in place somewhere else. Appellant was, however, able to secure a couple anchor tenants after giving some notable leasing concessions.

Though the shopping center does have some anchor tenants, the subject parcel itself has been unsuccessful in attracting tenants. Indeed, Appellant reported a vacancy rate of approximately 83% as of January 1, 2015. Appellant offered several factors which likely contributed to subject's inability to attract tenants. First, Appellant contended the development of the shopping center was ill-timed because the recession hit at the time Appellant was seeking tenants. Second, Appellant noted the demographics surrounding the shopping center were not as favorable as some of the other more successful shopping centers in the Treasure Valley. Appellant reported a population of roughly 30,000 within three (3) miles of subject with a median income of $41,000, both of which are less than many of subject's competitors. Lastly, and most importantly, Appellant explained subject suffers from considerable functional obsolescence. Rather than a traditional layout where smaller tenants face the anchor stores, which in turn draws traffic to the smaller retailers, the subject buildings are configured to face each other with an outdoor common area providing access between the buildings. One problem with subject's design is the storefronts are not visible from the main thoroughfare. Rather, cars passing by are only able to see the back side of the buildings, which does not help attract customers. Appellant detailed the efforts it has undertaken to try and lure tenants, including employing the services of at least four (4) local commercial brokers. Overall, subject and the shopping center itself have greatly underperformed.

The appraisal relied on the income approach to develop a value estimate for subject. In fact, two (2) income approach models were developed. The first was a direct capitalization model wherein net operating income was capitalized. The appraisal included one (1) notable extraordinary assumption; that subject was fully leased up to market levels. For income, the appraisal focused on subject's actual leasing history, as well as lease information from three (3) similar-type distressed shopping centers from the broader Boise/Nampa area. Median lease rates ranged from \$3.41 to \$15 per square foot. Subject's actual median lease rate is \$5.78 per square foot. In developing its value opinion, the appraisal used a \$7.75 per square foot lease rate. Expenses and other deductions were derived from the marketplace. The vacancy rate, however, was given special consideration. Focusing on the three (3) competitors referenced above, the appraisal noted vacancy rates of roughly 40% for each. Recognizing 40% vacancy was high, the appraisal utilized a 20% stabilized vacancy rate for subject. The net operating income was capitalized at 8%, which was near the middle of the indicated range. The result of the direct capitalization approach was a value conclusion of \$10,655,000.

Acknowledging the extraordinary assumption above did not represent reality, the appraisal developed a discounted cash flow model to reflect subject's "as-is" value. The appraisal determined a holding, or lease-up, period of ten (10) years, which was noted to be roughly double the actual absorption rate during subject's first eight (8) years of operation. Because most of subject's shop spaces are unfinished shells, the cost of tenant improvements was included in the analysis at a rate of $40 per square foot. A 10% discount rate was used due to subject's high vacancy rate and the higher level of risk associated with leasing up the spaces. The analysis yielded a total "as-is" value of $3,130,000.

Though Respondent questioned some of the inputs in the appraisal's direct capitalization model, the analysis was regarded as reasonable and acceptable. Therefore, Respondent did not present an alternative income approach.

Respondent did not agree, however, with the discounted cash flow analysis. Respondent suggested management was responsible for subject's poor performance, and thus contended no adjustment should be made for subject's atypically high vacancy. Appellant countered much time, effort, and expense has been spent trying to attract tenants to subject. Appellant noted it has hired at least four (4) different local commercial real estate brokers over the past several years in an attempt to lease subject's space. Appellant also remarked it has offered free rent and other concessions to potential tenants, but such efforts have not been successful. Appellant also reported contemplating converting the shopping center into an outlet mall, however, studies suggested such a change was not feasible. Overall, Appellant explained management has tried myriad methods of leasing subject, to no avail. In Appellant's view, subject's poor performance is directly related to unfavorable demographics and its unconventional design.

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, or as applicable exempt status. This Board, giving full opportunity for all arguments and having considered all testimony and documentary evidence submitted by the parties in support of their respective positions, hereby enters the following.

Idaho Code § 63-205 requires taxable property be assessed at market value annually on January 1; January 1, 2015 in this case. 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.

There are three (3) generally-accepted methods for determining market value: the income approach, the cost approach, and the sales comparison approach. *Merris v. Ada County*, 100 Idaho 59, 63, 593 P.2d 394, 398 (1979). In this case, the parties relied on the income approach, which is common for valuing income-producing properties.

Appellant offered a fee appraisal of subject in support of reducing the assessed value. The appraisal developed two (2) income approaches, a direct capitalization model and a discounted cash flow model. Respondent agreed with the analysis and value conclusion reached in the direct capitalization model, however, contested the discounted cash flow analysis. Respondent reasoned because assessed values are determined on a retrospective basis, it should not consider a forward-looking valuation, which is what a discounted cash flow analysis does. Appellant countered even the direct capitalization model includes some consideration of the future, such as determining a capitalization rate. Appellant argued the discounted cash flow should be considered because the value conclusion reached using the direct capitalization model made the extraordinary assumption subject was occupied at market levels, which is not the case, nor will it be the case in the near future. Further, the discounted cash flow method factored in the significant lease-up costs associated with trying to fill subject's retail spaces. Currently the unoccupied space is in shell condition and a buyer of the subject property would factor in the costs of adding tenant improvements. Extraordinary efforts have been made to lease subject's spaces, yet subject's performance continues to languish. This suggests subject suffers from functional obsolescence and perhaps other detriments. It follows then, consideration of subject's actual performance should be included in determining its value.

While the Board understands a market value opinion is naturally based on market data, so too must consideration be given to a property's functional use and historic performance. In this case, subject suffers from 83% vacancy, which high vacancy has persisted since subject's construction in 2007. In order to improve the occupancy a significant amount of time, money, and effort must be employed. This reality would not be lost on a buyer who would likely be looking at subject's revenue-generating potential. The costs and risks associated with improving subject's performance negatively impacts its market value. Respondent failed to account for subject's inherent difficulties, which was viewed by the Board as a fatal flaw in Respondent's value position.

According to Idaho Code § 63-511, Appellant bears the burden of proving error in subject's assessed value by a preponderance of the evidence. Given the information provided in record here, the Board is satisfied the burden of proof has been met. Appellant's analysis was regarded as superior to that offered by Respondent, and the value conclusion was well supported. As a result, the decision of the Canyon County Board of Equalization is reversed to reflect a total value of $3,130,000.

FINAL ORDER

In accordance with the foregoing Final Decision, IT IS ORDERED that the decision of the Canyon County Board of Equalization concerning the subject parcel be, and the same hereby is, REVERSED, to reflect a decrease in subject's total value to $3,130,000.

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 29th day of April, 2016.