BEFORE THE IDAHO BOARD OF TAX APPEALS

IN THE MATTER OF THE APPEAL OF NEIBAUER CHUBBUCK HOLDINGS, LLC from a decision of the Bannock County Board of Equalization for tax year 2013.	))))	APPEAL NO. 13-A-1150 FINAL DECISION AND ORDER

COMMERCIAL PROPERTY APPEAL

THIS MATTER came on for hearing November 4, 2013, in Pocatello, Idaho before Hearing Officer Travis VanLith. Board Members David Kinghorn, Linda Pike and Leland Heinrich participated in this decision. Attorney David Crapo appeared at hearing for Appellant. Assessor David Packer and Appraiser Randy Larsen appeared for Respondent Bannock County. This appeal is taken from a decision of the Bannock County Board of Equalization (BOE) modifying the protest of valuation for taxing purposes of property described by Parcel No. RCRG2000100.

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

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

FINDINGS OF FACT

The BOE assessed land value was $1,895,559, and the improvements' valuation was $14,635,725, totaling $16,531,284. Appellant requests the total value be reduced to $12,550,000, by reducing the improvements' valuation to $10,654,441, and making no change to the land value.

The subject property is a 78,225 square foot commercial building situated on a 9.46 acre parcel in Chubbuck, Idaho. Constructed in 2011, the building interior consists primarily of open cubicle-type space with limited space reserved for private offices. The building also houses a cafeteria, training rooms, lockers and showers, and two (2) break rooms. Respondent noted subject was recognized as an environmentally friendly building. Exterior improvements include sprinklers, lighting, and paved parking for roughly 500 cars.

Appellant reported details on subject's history. The current tenant, a national company, desired to open a call center in the area some time ago. The tenant, however, did not want to finance the land acquisition and construction costs to build the facility. Therefore an agreement was reached with a developer whereby the developer would acquire the land and construct the building. The tenant agreed to execute a 10-year lease agreement with two (2) renewal options. The developer installed the exterior improvements and constructed the building, which mostly resembled a shell, in September 2011. A total of $14,889,346 was spent to purchase the subject lot and build the improvements, which was considerably less than the anticipated cost of $21,205,187. The tenant was responsible for additional interior improvements. The most notable such improvement was a raised floor to allow for computer and telephone wiring to be out of sight, yet easily accessible.

In October 2011, the developer sold subject to another party for $11,091,000. In September 2012, an offering memorandum was issued for subject. On October 23, 2012, Appellant's purchase offer of $12,550,000 was accepted and the property went into escrow. The transaction closed on January 18, 2013 and was recorded January 24, 2013. Appellant asserted a reasonably prudent buyer in the market would have been aware of subject's October 2012 contract. As such, Appellant contended the purchase price should be a primary indication of subject's value on the January 1, 2013 lien date.

In support of reducing subject's assessed value, Appellant also offered valuations derived from each of the three (3) generally accepted appraisal approaches. The sales comparison approach considered the two (2) above-referenced sales of subject. The most recent sale was regarded as most reflective of subject's current fair market value, so a value of $12,550,000 was concluded.

Appellant also offered two (2) income approach analyses. The first was an income capitalization approach. Subject's actual rents of $12.27 per square foot were used, as were vacancy and expense rates of 0% and 5%, respectively. The 7.5% capitalization rate was taken from data contained in a recent edition of a trade publication. The value conclusion using this direct income method was $12,052,000.

Appellant's other income approach was a discounted cash flow analysis, or yield capitalization model. This approach looked at the expected future income and discounted it back to present-day value. Using subject's actual rents, which increase 1.5% per annum pursuant to the terms of the lease agreement, and an 8.7% discount rate, Appellant calculated an income figure for the first 10 years of $1,051,879. A residual capitalization rate of 8.03% was used for the later income, resulting in a total present value of $12,338,918.

Lastly, Appellant presented a cost approach. Using the Marshall & Swift cost manual, Appellant valued subject's various components. The building was considered an average Class C building, which equated to a cost new rate of $98.36 per square foot. After making adjustments for height, depreciation, and exterior improvements, Appellant determined a final value of $11,154,000. Respondent noted the offering memorandum described subject as a Class B building. Appellant recalculated subject's value using the Class B value rate, resulting in a value of roughly $14,700,000.

Appellant regarded subject's most recent purchase as the best evidence of current value. Of secondary importance were the income approach conclusions. While Appellant provided a cost approach, it was argued the method was not a reliable indicator primarily because a potential buyer would likely be more interested in the income-producing or resale potential of the property. Appellant petitioned little or no weight be afforded the cost approach.

Respondent likewise considered the three (3) approaches to value. The cost approach first looked to three (3) sales of unimproved commercial parcels. The first two (2) involved 4.37 and 13.23 acre parcels which sold respectively in 2005 for $1,142,140 and in 2008 for $3,321,337. The third sale was the purchase of subject's lot for $2,060,385 in 2011. Respondent concluded subject's purchase was the best indicator of land value.

Concerning subject's improvements, Respondent also used the Marshall & Swift cost manual. Respondent considered subject an excellent Grade B building with a base valuation rate of roughly $225 per square foot, after other adjustments were applied. Respondent calculated a value of $17,000,000 for subject's improvements, and a total property value of $19,060,390.

Respondent's sales comparison approach considered four (4) improved commercial sales, one of which was subject's recent purchase for $12,550,000. Sale No. 1, located in Salt Lake City, Utah, sold in May 2012 for $30,000,000, or $147.80 per square foot. The 9.77 acre parcel was improved with a 202,972 square foot office building which was remodeled in 1996. Appellant reported this sale property provides deluxe office space for professionals, such as attorneys and accountants. The building was also noted to host wedding receptions on occasion. In Appellant's view, the sale property was far superior to subject in terms of interior finish.

Sale No. 2 involved a 5.82 acre parcel located in Everett, Washington. According to the listing sheet, the parcel was improved with two (2) office buildings. The larger three (3) story building contained 71,780 square feet, and the other two (2) story building consisted of 40,128 square feet. The property sold in June 2012 for $20,425,000, or $182.52 per square foot. Appellant mostly questioned the comparability of this sale in terms of its more suburban location compared to subject's Chubbuck locale.

Respondent's third sale closed in December 2012. The 9.22 acre South Jordan, Utah property, improved with a 123,908 square foot building, sold for $48,400,000, or $390.61 per square foot. Appellant noted the property is owned and used as a medical building for a local university. Appellant opined the interior finish of such a building far exceeds that of subject's.

Respondent provided an income approach using a yield capitalization model. The present value of subject's projected income stream for the next ten (10) years was calculated. Added to this was the Year 11 income capitalized at 6.5%. Respondent calculated a total present value of $17,344,450.

Appellant identified an error in Respondent's calculation which significantly impacted the value conclusion. Respondent indicated a Year 11 income of nearly $1.9 million, however, the actual income should have been $1,028,245. After incorporating the new income figure, the total present value conclusion was reduced to approximately $12,000,000.

Respondent weighted its value conclusions as follows: 40% income approach, 40% cost approach, and 20% sales comparison approach. Less weight was placed on the sales comparison approach because Respondent did not have enough physical details concerning the sale properties to make proper appraisal adjustments for comparison with subject. Respondent determined a value of $16,412,796 for subject's improvements, and $2,060,390 for the land, totaling $18,473,186. Respondent petitioned subject's value be increased to this new value.

Respondent further provided details on subject's building permits throughout the construction process. A permit for the foundation was issued in December 2010 with a permit value of $1,375,000. A March 2011 permit value for the building's shell was $5,325,437, and the subsequent interior permits totaled $9,681,383. In all, permit values totaled $16,381,820, which Respondent noted did not include the underlying land. Respondent viewed this information as another indicator of subject's probable value being in the $18 million range.

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 all taxable property be assessed at market value annually on January 1 of the relevant tax year. 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.

The Idaho Supreme Court has identified three (3) primary methods for determining market value, ". . . the cost approach . . . the income approach . . . and the [sales comparison] approach, in which value of the assessed property is ascertained by looking to current open market sales of similar property." *Merris v. Ada County*, 100 Idaho 59, 63, 593 P.2d 394, 398 (1979). Both parties offered value opinions for subject that considered the three (3) methods described above, though the respective value conclusions differed.

In addition to the above appraisal approaches, Respondent provided additional information concerning the building permits issued for subject's development. The permit values totaled more than $16 million. Respondent also reported subject's development budget was nearly $22 million. Appellant reported the actual development costs were $14,889,346, which included the purchase of subject's 9.46 acres for $2,060,385 in January 2011.

While details related to building permits and budgets is interesting information, such are not recognized as reliable indicators of market value. Permit values and cost projections are not estimates of market value. In this case, the early estimates proved to be erroneous as evidenced by the actual development costs, which were notably lower than anticipated.

The parties' cost approach analyses were mostly similar. The biggest difference was in the class and type categories used to calculate the basic structure replacement cost. Appellant offered values for subject as both a Class C and Class B building, with a type-rating of "Average". The value conclusions were roughly $11 million and $14.7 million, respectively. In contrast, Respondent considered subject a Class B structure with a type-rating of "Excellent", which is the highest available rating. Respondent concluded an improvement value of $17,000,000, or a total property value of $19,060,390 using the cost approach.

Appellant contended the cost approach was the least reliable valuation method in this case. Appellant opined that a potential buyer would be looking at either subject's income-producing ability or its resale potential, not historical development cost information. Respondent argued cost was important because subject may not necessarily sell as an income-producing property. On the relevance of the cost approach, the Board found Appellant's position more reasonable and supported.

The cost approach can be a useful tool in ascertaining market value, particularly for a common and recently-constructed property. While subject was recently constructed, the Board did not view the cost approach as most indicative of its market value. Throughout its short history, and continuing through January 1, 2013, subject has been purchased for both its income and resale potential. Now that the building has been finished and has been trading in the market, the construction costs are less meaningful.

Another area of concern for the Board was the divergent value conclusions reached under the cost approach. The parties generally agreed subject is a Class B building, but did not concur on the building's type-rating. From the information presented, the Board is unable to determine which rating more accurately represents subject. The Board was further concerned that Respondent's cost approach conclusion was approximately $4 million more than subject's actual construction costs. Overall, the Board viewed the parties' cost approaches with caution.

The Board held the parties' income approach conclusions in higher regard. The input factors were similar between the parties, though there was some variation in the respective capitalization rates. Appellant offered two (2) income approaches, both of which concluded a total value around $12 million. Respondent's initial yield capitalization model determined a value of roughly $17 million, however, an error was discovered in the calculation. After adjusting Year 11 income to a more suitable amount, Respondent's approach indicated a value of just under $12 million. Due to the overall similarity of the parties' models in terms of the input factors and the final value conclusions, the Board viewed the income approach as an important value indicator in this case.

The parties varied the most in their respective sales comparison approaches.

Respondent provided three (3) commercial property sales from 2012. The sale properties ranged in size from 111,908 to 202,972 square feet and in acreage from 5.82 to 9.77 acres. The properties sold for between $20,425,000 and $48,400,000. Respondent concluded a value of $19,556,250 for subject based on the sales.

The Board had several concerns with Respondent's sales comparison approach. Most importantly was the lack of comparability between the sale properties and subject. Each of the sales was located outside Idaho and the buildings were all notably larger than subject. Though physical details were scant, Appellant noted the Utah sales involved buildings with a much higher degree of interior finish than subject. Respondent acknowledged details on the sale properties were lacking, which hampered its ability to make appraisal adjustments typically involved in the sales comparison approach. The inability to directly compare the sale properties to subject, and to make the indicated adjustments, undermined the reliability of Respondent's sales comparison approach.

Appellant did not offer a traditional sales comparison approach. Rather than looking to recent, open market sales of similar property, Appellant relied on a consideration of subject's 2011 and 2013 purchases. Deeming the more recent purchase as most indicative of subject's current value, Appellant concluded a value of $12,550,000.

The sales comparison approach typically examines multiple sales of similar type property in an attempt to estimate the most probable price of the property being appraised. In most instances, the property being valued has not recently sold. Therefore, it is necessary to look to the market for comparable sales. In the instant case, however, the subject property went into escrow before the January 1, 2013 valuation date, and closed for that contract price soon thereafter. There was no indication the sale was distressed, or that the transaction was not at arm's-length. The only issue is the actual closing took place in 2013. Under the facts here, that concern is lessened by the fact the final sale price was negotiated and put under contract in October 2012. That the closing was not complete until January was viewed as irrelevant where the price was stated and acted upon well before the effective date of valuation.

Given the information presented, the Board is strained to find a better indication of subject's current value than its recent purchase. The parties' respective income approaches provided further evidence that the purchase price was reflective of fair market value. Accordingly, the decision of the Bannock County Board of Equalization is reversed to reflect a decrease in the value of subject's improvements to $10,654,441, with no change in the $1,895,559 land value.

FINAL ORDER

In accordance with the foregoing Final Decision, IT IS ORDERED that the decision of the Bannock 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 $12,550,000.

IT IS FURTHER ORDERED that 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.

DATED this 27th day of February, 2014.