BEFORE THE IDAHO BOARD OF TAX APPEALS

IN THE MATTER OF THE APPEAL OF ROCKWOOD CALDWELL OREG. LTD. from a decision of the Canyon County Board of Equalization for tax year 2013.	))))	APPEAL NO. 13-A-1118 FINAL DECISION AND ORDER

COMMERCIAL PROPERTY APPEAL

THIS MATTER came on for hearing October 21, 2013, in Caldwell, Idaho before Hearing Officer Travis VanLith. Board Members David Kinghorn, Linda Pike and Leland Heinrich participated in this decision. Attorney David Penny and witness W. Scott Phinney appeared at hearing for Appellant. Chief Appraiser Brian Stender, and Appraisers Mike Cowan and Darryl Speiser appeared for Respondent Canyon County. This appeal is taken from a decision of the Canyon County Board of Equalization (BOE) modifying the protest of valuation for taxing purposes of property described by Parcel No. 353490000.

The issue in this appeal is the market value of an apartment complex operating under the Section 236 low-income housing program.

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

FINDINGS OF FACT

The BOE reduced subject's assessed land value to $391,400, and the improvements' valuation to $908,600, for a total of $1,300,000. Appellant requests a total value of $800,000.

The subject property is a 48-unit low-income apartment complex built in 1972. The complex is made up of eight (8) buildings possessing 1, 2 and 3 bedroom units. Subject is located in Caldwell, Idaho, near the College of Idaho.

On January 1, 2013, subject was operating as a low-income housing project.

Residents included Housing and Urban Development Act ("HUD") Section 236 and Section 8 housing tenants. HUD Section 236 was abandoned by the federal government in 1973. It has since been replaced by Section 8 and Section 42 housing programs. By default, when the operation of a Section 236 housing project expires, it reverts back to a "market" apartment property. Subject will come out of its Section 236 HUD housing program in April of 2013 with no option to re-enter.

Because of subject's age, Appellant reported there were deferred maintenance and obsolescence issues which must be considered in the valuation. The cost to cure these issues was estimated to be between $250,000 and $300,000. Subject was also noted to have a 25% vacancy rate. Further discussed were demographics of Caldwell and the surrounding area. It was suggested subject's location further dictates a decreased value.

Appellant argued to properly value subject, the property's actual and functional use must be considered. The government program restrictions concerning low-income housing were described in detail. When the Section 236 program was initiated, strict restrictions were placed on projects like subject's. Tax incentives were offered to developers of such projects. In return for the incentives, restrictions were placed on the operation of the developments and the financial benefits that could be obtained from ownership. Only restricted rents could be charged for the individual units and tenants had to meet low-income qualifications in order to live in the project.

The owners of Section 236 housing were required to place monies into replacement reserves each month and were limited to a maximum annual dividend or income distribution. In subject's case, $10,090 was the maximum distribution allowed. As part of a Section 236 agreement, many other restrictions and expenses are mandated. Section 8 was described as another program which gives vouchers to qualifying tenants with which to pay the Section 236 rents.

In its appraisal, Appellant looked to all three approaches to value. The cost approach was rejected where it was deemed too subjective due to subject's age and condition. Using the income approach, subject's operating history was analyzed. Appellant offered testimony that since there was a negative net operating income, the indication was that subject had no value. The rents were stated to be low because of the restrictions related to the Section 236 program. The vacancy rate was said to be high based on the condition of the property and due to the competition from newer and nicer properties available in other low-income housing projects.

Due to the forgoing analysis, Appellant used an alternative income approach. Actual vacancy was replaced with a market vacancy rate of 5%. Using this approach, indicated a value for subject of $442,500. This calculation included a deduction for replacement reserves required by the federal regulation. Apart from making the reserves deduction, a value of $752,360 was indicated.

In the sales comparison approach, there being no sales of Section 236 properties, Appellant provided information on four (4) sales of market rent apartments. The sale properties were located within the surrounding area. Appellant analyzed the sales to determine a ratio of its restricted rents compared to the market rents, then applied the ratio to the indicated price per unit observed in the four (4) sales. The special modeling indicated an average value of $23,746 per unit for subject's 48 units. The total value, after making a deferred maintenance adjustment was $889,808. Respondent contended supporting details were lacking on the four (4) sales and argued the sales should be disregarded.

Appellant put most emphasis on its income approach because an investor would be primarily concerned with the property's income potential. In the income approach, a direct capitalization method was used largely in conjunction with subject's restricted-rent operating history. The net operating income before capitalization and after deducting for replacement reserves was $55,289. A measurement of actual rents was used together with a market vacancy factor of 5%. The overall capitalization rate of 8% was based on a regional survey. Appellant deducted $250,000 for deferred maintenance. The final value concluded in the income approach was $752,360.

After reconciliation of the value indicators, with more weight put on the income approach, Appellant determined a final value of $800,000.

Respondent explained its consideration of subject's value, noting the apartment units were not well maintained in recent years. It was generally agreed the units required some maintenance work to be competitive in the local market. The deferred maintenance issues were said to be duly considered in the county's final value conclusion.

Respondent reported on the current assessment date of January 1, 2013, subject was bound by Section 236 and Section 8 HUD housing regulations. However, it was noted that on this valuation date the owner knew subject would soon be exiting the Section 236 program. It was opined a prospective buyer would purchase subject primarily in anticipation of being outside the constraints of the programs. Therefore, subject's actual and functional use outside of the program was also considered in Respondent's valuation.

Respondent characterized subject as a "transitioning property" and placed its emphasis on a consideration of the recent comparable sales of market rent units. Appellant countered that on January 1, subject was still controlled by the Section 236 operating agreement and should be valued accordingly.

Respondent also considered the three (3) traditional approaches to value. It was declared the cost approach was unreliable in determining market value due to subject's age. Respondent suggested the income approach was not reliable due to the limited amount of market income data available. It was contended the income information provided by Appellant did not reflect the key fact that subject would be coming out its HUD program. In Respondent's judgment it was not reasonable to use the income approach in the current valuation.

Respondent deemed the market approach provided the most reliable comparative data for valuing subject. Information was provided on sales of government subsidized apartments, along with information on sales of regular "market rent" apartments. The sales were said to be of similar age, size and unit mix as the subject. In all, information on eight (8) 2012 sales was offered. In the two (2) types of sales, four (4) were government subsidized apartment sales and four (4) were local "market" apartment sales. The four (4) subsidized rent sales ranged in size between 27 and 51 units and had sale prices between $945,000 and $1,700,000. The per unit prices ranged between $27,020 and $42,500, with the average rate being $33,483.

The subsidized rent sales were located in Lewiston, Twin Falls, and Payette, Idaho, and one (1) property was located in Helena, Montana. Appellant discounted these sales because Respondent made no location adjustments. Secondly, Appellant argued a consideration of the sales was problematic where Respondent did not know the specifics of the government programs and did not know the conditions surrounding the sale transactions.

Respondent's four (4) local, market rent apartment sales ranged in size from 9 to 41 units. Sale prices were between $300,000 and $1,440,000, and the indicated average per unit price rates between $27,273 and $45,000. Respondent regarded Sale No. 1, located in Nampa, Idaho, as most similar to subject. At the time of sale, the property had deferred maintenance issues, mostly where two (2) of the units were damaged by fire. The complex was built the same year as subject and the total unit count was 41. Further, the Sale No. 1 property used construction materials similar to subject's and the property was located near a university, like subject. This property sold for $1,440,000, or $35,122 per unit, in May of 2012.

Respondent held "the subject property compares more closely with the market rent unit comparable sales versus the HUD program's comparable sales." This was asserted where subject would exit the Section 236 program by default and then revert to a complex of market rent units. Based on the coming reversion, the County argued it was invalid to rely on historic income in estimating subject's current market value.

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.

The tax law requires market value be estimated giving major consideration to a property's actual and functional use. Section 63-208, I.C.; *Greenfield Village Apartments, L.P. v. Ada County*, 130 Idaho 207, 938 P.2d 1245 (1997). In the assessment and valuation of "rent-restricted" apartments some consideration of contract rents is therefore made.

Subject is used as an income producing property. It is the expected future income that drives its present value. On the January 1, 2013 assessment date, subject had about four (4) months of its future income specially limited by a HUD operating agreement. The agreement restricted rents and controlled other aspects of the property's use. After this relatively brief period, the apartments would then operate as market-rent units. Giving consideration to subject's actual and functional use would entail considering both the relatively brief restricted rent period and the longer future market rent period.

In its valuation of subject, Respondent characterized the property as a transitioning property. From Appellant's perspective it would take years to complete the transition into a market rent apartment. Appellant consequently put forward an appraisal that relied heavily on the income approach, which approach was largely based on subject's income under the rent restricted scenario. After deducting $250,000 for deferred maintenance, the resulting valuation of income was $752,360.

In contrast Respondent relied mainly on a consideration of recent sales, i.e. the sales comparison approach. The approach primarily looked to the sale prices of market-rent apartments. Of the four (4) local "market" sales, Respondent noted one (1) was highly similar to subject. The sale property's characteristics included deferred maintenance issues, the same year built as subject, 41 total units, the same or similar construction materials as subject, and a location near a university. The property sold for $1,440,000, or $35,122 per unit, in May of 2012. By comparison, subject's assessment indicated an average rate of $27,083 per unit.

The fact that subject was assessed considerably below the price rate for the above sale, suggests to this Board, that the deferred maintenance issues and subject's restricted rents into April of 2013 have been duly considered.

Key to the Board's final decision here was the fact subject's use under a 40-year operating agreement would end on approximately April 1, 2013. From this point forward, the property considered in a fee simple interest would be similar to that of a consideration of an investment in a market rent property. After its termination from the Section 236 program, it is the Board's decision that subject's income and value should be considered for assessment purposes like other apartment complexes free to seek market rents.

On the 2013 assessment date, subject would legally operate as a rent-restricted property for a brief period. This factor could be considered in different ways within each of the appraisal approaches. Critical to the analysis would be recognizing that the special restrictions would be in place for less than four (4) months. After this period, the appraisal of future income should be based on a consideration of market rent. Subject will likely experience a transition period as it switches over to a market rent operation. The fact that subject may have some delays or encounter special costs in making the transition should not effect its appraisal under a market rent scenario.

Neither party sought to distinctly or separately value subject's two (2) future income elements. Appellant effectively projected the restricted-rents treatment well into the future. Respondent generally pursued subject's current value through a comparison to sales of market rent units. Where subject will only be rent-restricted for a short time, Respondent's market value consideration was judged to be closer to the mark. Respondent's case was the more reasonable where it also evaluated subject's overall physical condition, the rent-restricted nature of the property, and the available info on subject's actual income.

In conclusion, on the valuation date subject would soon end its association with the Section 236 program and the requirements of the operating agreement. Some consideration was due the fact subject still had a couple months to run under the HUD housing agreement. On review, we found the BOE valuation of subject demonstrated a reasonable consideration of this fact and also gave due consideration to the key driving value factor which was subject's presence within the marketplace of market rent apartments.

Appellant's valuation was not found to have made a reasonable consideration of subject's future. Appellant did not present a superior valuation to that offered by Respondent. Regarding the County's assessment no error was proven.

For the reasons expressed above, the decision of the Canyon County Board of Equalization will be affirmed.

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, AFFIRMED

DATED this 25th day of March, 2014.