

BEFORE THE IDAHO BOARD OF TAX APPEALS

WEST VALLEY MEDICAL CENTER, INC.,	)	
	)	
Appellant,	)	APPEAL NO. 16-A-1089
	)	
v.	)	FINAL DECISION
	)	AND ORDER
CANYON COUNTY,	)	
	)	
Respondent.	)	
_____	)	
	)	
	)	

**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. 029440000. The appeal concerns the 2016 tax year.

This matter came on for hearing December 7, 2016 in Caldwell, Idaho before Hearing Officer Travis VanLith. Attorney Clint Bolinder represented Appellant at hearing. Chief Deputy Assessor Joe 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 \$1,540,500, and the improvements' value is \$17,979,500, totaling \$19,520,000. Appellant contends the correct total value is \$13,500,000.

The subject property is a 6.43 acre parcel improved with a hospital roughly 150,000 square feet in size. The hospital was constructed in 1977 and since that time has experienced several additions and renovations. The hospital is licensed for 150 beds, however, 99 beds are currently staffed and operating. The property is further improved with a 14,116 square foot

administrative building constructed in 1969 and commonly referred to as the Kaley Building.

In 2015, work was completed on a new surgery center and a cardiac catheterization lab which added about 7,461 square feet to the hospital facility. A local newspaper article reported project costs of \$9.25 million, however, Appellant explained that figure represented the total investment, including major medical equipment. Appellant reported building construction costs were approximately \$5 million. Due to the difficulties and high expense associated with renovating an active hospital, Appellant explained such construction costs typically exceed the contributory value of the new improvements. In other words, cost does not necessarily equal value. Such was argued to apply to subject's new improvements, which Appellant estimated contributed roughly \$3 million to the property's overall value.

In support of its value position, Appellant offered into evidence an independent fee appraisal of the subject with a January 1, 2016 valuation date. The fee appraisal described some issues negatively impacting subject's value. First, the appraisal noted about 70% of a hospital's current revenues come from providing outpatient services, which is a dramatic shift from past markets wherein inpatient services provided the bulk of revenues. Subject's design, being an older hospital, is not well-suited for the outpatient services trend. Many of subject's patient rooms were designed for double-occupancy, whereas today's market prefers single-occupancy rooms. This was offered to partially explain why only 99 of 150 licensed beds are staffed.

The appraisal also noted subject's location in a residential neighborhood, somewhat away from the freeway. It was explained with increased outpatient services, hospitals are building near freeways and major access corridors to provide increased convenience to patients. In this

regard, the appraisal pointed to a couple new, local hospitals being constructed near Interstate 84. In Appellant's opinion, subject would not be constructed in its current location if it did not already exist.

The fee appraisal relied on the cost and sales comparison approaches to value. The income approach was excluded where hospitals are not typically leased independent of the business, and finding lease information was deemed too difficult. The appraisal's cost approach first developed a land value opinion. Five (5) vacant lot sales were considered. Lot sizes ranged from .42 to 7.76 acres. Sale prices were between \$94,900 and \$950,000, or from \$2.81 to \$5.80 per square foot. After adjustments for time, location, size, and zoning, adjusted sale price multiples ranged from \$3.37 to \$4.56 per square foot. The appraisal concluded a value rate of \$4.00 per square foot, or \$1,120,000 for subject's land.

Turning to the value of the hospital building, the fee appraisal considered construction cost information from eight (8) hospital projects, as well as cost data from Marshall Valuation Service (MVS). The adjusted costs for the eight (8) hospital comparables ranged from \$270 to \$429 per square foot, with a median adjusted cost of \$321 per square foot. Because the subject hospital is notably smaller than the comparables, and the average size per patient bed is only 987 square feet compared to the hospital comparables with average sizes ranging from 1,763 to 3,075 square feet per bed, the appraisal estimated a replacement cost new between \$270 and \$290 per square foot for subject's hospital facility. Using MVS, the appraisal valued subject as a Class A - Average Quality General Hospital. The appraisal noted an average-type hospital, according to MVS, has an average of 1,125 square feet per bed. As a result of subject's average per-bed size being smaller, the appraisal estimated a replacement cost range between

\$280 and \$285 per square foot. In reconciling the value indicators, a replacement cost new for subject's hospital facility of \$285 per square foot, or approximately \$42 million was concluded.

In determining the depreciation factor, the appraisal relied on the age-life method, which in basic terms calculates depreciation from all sources in a single step. This method calculates the ratio between the effective age of an improvement and the total economic life expectancy and applies the ratio to the estimated replacement cost new. The fee appraisal cited three (3) sources used to determine the subject hospital's life expectancy. The first was a study of hospitals which have been replaced. Ages at the time of replacement ranged from 23 to 45 years, with a median age of 36 years. The second life expectancy source was MVS, which indicated a typical life expectancy between 35 and 50 years for an acute care hospital. Lastly, the American Hospital Association reported a useful life ranging from 25 to 40 years. A 40 year life expectancy was determined for subject hospital. The appraisal estimated the subject hospital's effective age at 28.1 years, which after dividing by the 40 year life expectancy, resulted in a 70.2% depreciation factor. Applying this to the estimated replacement cost new yielded a rounded value of \$12,430,000. Adding \$550,000 for the value of the Kaley Building, plus the \$1,120,000 land value, the fee appraisal concluded a total value of \$14,100,000 for all of the subject property.

In its sales comparison approach, the fee appraisal considered information on five (5) hospital sales. Three (3) of the sales occurred in 2015 and two (2) were from 2010. Most of the sale properties were larger than subject in both land and building size. Also, at 987 square feet, subject's average patient room size was notably smaller than all the sale properties. After removing land values, indicated prices for the improvements ranged from \$4,817,286 to

\$32,480,000, or between \$43.32 and \$76.24 per square foot. Adjustments were made to account for differences in location, size, and quality. The adjusted prices ranged from \$58.48 to \$80.05 per square foot. The appraisal determined a value for the subject hospital of \$70 per square foot, or \$10,370,000. After adding the land value and the value attributable to the Kaley Building, a total value of \$12,040,000 was calculated. Reconciling the two (2) approaches to value, the fee appraisal concluded a total value of \$13,500,000.

Respondent's analysis similarly excluded the income approach, also relying on the cost and sales comparison approaches to value. Respondent first listed all remodels or additions made to the property since 1996, according to building permit records. The total value of the permits was noted to be roughly \$19.8 million. Respondent next estimated subject's effective age at 25.1 years by using the weighted ages of the various components of the hospital. These components included the additions made to the hospital since its construction in 1977, as well as several remodeling projects completed through the years. Appellant pointed out the total square footage of the additions and remodels in Respondent's chart was roughly 219,000 square feet, whereas subject's actual total size is about 150,000 square feet. Appellant argued it was improper to include renovations in calculating a weighted age, but that such should be included in estimating the effective age. Respondent acknowledged some of the remodel work overlapped other remodel work, however, maintained the renovations should be included in calculating subject's weighted age.

For the replacement cost new (RCN) estimate, Respondent relied on MVS, as well as reported construction cost data on two (2) local hospitals. Subject was considered a Class A - Average General Hospital for purposes of MVS. After making adjustments to the base rate of

\$280.61 per square foot, Respondent estimated an RCN rate of \$292 per square foot for subject. Respondent also referenced construction costs of \$466 and \$333 per square foot related to two (2) local hospitals. Respondent equally weighted the MVS rate of \$292 with the reported cost of \$333 per square foot for the new local hospital regarded most similar to subject, and concluded an RCN estimate of \$313 per square foot, or \$47,329,356.

Respondent next examined subject's useful life. Respondent cited a summary of a hospital study posted online. The posting suggested a useful life range between 40 and 50 years for hospitals. MVS suggested a 45-year typical useful life for an average quality Class A hospital. With an effective age of 25.1 years and an expected useful life of 45 years, Respondent calculated a depreciation factor of 55.8%. The result was a depreciated value of \$20,900,000 for the hospital. Adding \$560,000 for the Kaley Building and \$1,540,500 for the land, Respondent concluded a total value of \$23,000,000 under the cost approach.

Offered in support of Respondent's land value conclusion of \$1,540,500 was information concerning five (5) vacant lot sales. Lot sizes ranged from 1.03 to 13.53 acres, with sale prices between \$750,000 and \$ 5,620,000, or between 4.08 and \$16.72 per square foot. After making adjustments for location and size, adjusted price rates ranged from \$4.89 to \$11.70 per square foot. Respondent determined a value of \$5.50 per square foot for subject's land.

Respondent's sales comparison approach included information on four (4) hospital sales and one (1) medical center sale which occurred between 2010 and 2013. Respondent reported sale prices for the hospital ranged from \$12,916,000 to \$60,000,000, or from \$102 to \$229 per square foot. After making adjustments for age, size, and date of sale, adjusted price rates between \$112 and \$275 per square foot were determined. The medical center property

reportedly sold for \$25,000,000, or \$214 per square foot. After adjustments, Respondent calculated a price rate of \$169 per square foot for the medical center property. Respondent concluded an average value rate for the subject of \$212 per square foot, or \$35,600,000. Reconciling the two (2) approaches to value, Respondent determined a final total value of \$25,320,000 for the subject property.

Appellant questioned some of Respondent's sales data, particularly the reported sale prices. According to Respondent, Sale Nos. 1 and 2 sold for roughly \$48 million and \$13 million, respectively. Appellant explained the reported prices were total purchase prices, which included significant amounts of intangible and equipment value. According to Appellant's information, the allocated prices for the real property components were about \$17 million for Sale No. 1 and \$5 million for Sale No. 2. Appellant also highlighted a square footage error concerning Sale No. 5. Respondent reported the facility size at 285,107 square feet, however, Appellant offered testimony the hospital exceeded 400,000 square feet in size, which would reduce the adjusted price per square foot from \$240 to roughly \$171.

#### 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, 2016 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.

Market value is estimated according to recognized appraisal methods and techniques. The sales comparison approach, the cost approach, and the income approach represent the three (3) primary methods for determining market value. *Merris v. Ada County*, 100 Idaho 59, 63, 593 P.2d 394, 398 (1979). Both parties developed value opinions using the sales comparison and cost approaches.

The Board understands the difficulty associated with valuing a special use property like subject and the parties' efforts in this regard were appreciated. As both parties developed value expert opinions using the same approaches to value, the question here becomes which value opinion was better supported and reflected a more accurate estimate of subject's current market value. For the reasons expressed below, we found Appellant's value conclusion more thoughtful, thorough, and better supported.

Looking first at the sales comparison approach, both parties relied on five (5) sales. Two (2) of the sales were used in both parties' analyses, however, the reported sale prices were widely divergent. Respondent reported the sale prices at roughly \$48 million and \$13 million. Appellant argued the prices reported by Respondent were overall sale prices including value attributable to other property like equipment. According to the filed Medicare cost reports, the allocated prices for just the real property were approximately \$17 million and \$5 million, respectively. Respondent questioned the accuracy of these reported prices and maintained the total sale prices did not include intangible property and equipment values. This position is

difficult to accept considering both hospitals were purchased as going-concerns. In the Board's experience, the purchase price of an active income-producing property can include value attributable to different business assets, which values often would be excluded when appraising only the real property. Whether the price allocations reflected in the Medicare cost reports are 100% accurate is impossible to determine from the record, however, Respondent's failure to account for, or consider, the presence of possible other property included in the total sale is deemed a significant flaw.

The Board was also concerned with other aspects of Respondent's sales comparison approach. First, Sale No. 4 involved a "medical center", not a hospital. The parties agreed this property was not directly comparable to subject. Also of concern was the size of the hospital involved in Sale No. 5. Respondent indicated a total size of approximately 285,000, however, Appellant reported the hospital exceeded 400,000 square feet. Lastly, the Board was strained to understand how the sales comparison approach at \$35,600,000 correlated with the property's assessed value of \$19,520,000. We also found this sales comparison approach value to be nearly \$13,000,000 more than the value conclusion reached in the cost approach.

Appellant's sales comparison approach was better received by the Board. Full details concerning each sale property were provided, including breakdowns of the improvements associated with the sales and other pertinent information. The adjustments were straight forward and reasonable on their face, and the value conclusion of \$12,040,000 fit well within the range indicated by the sales.

Turning to the cost approach, the parties' respective analyses were largely similar, however there were a few key areas of departure, which resulted in markedly different value

conclusions. The first key difference was the replacement cost new (RCN) rate. Respondent, relying on MVS and construction cost data concerning two (2) local hospitals, concluded a RCN of \$313 per square foot for subject. Appellant's concluded RCN rate of \$285 per square foot was based on cost data concerning eight (8) hospital projects and MVS, with special consideration given to subject having less square feet per patient bed. Subject's 987 square feet per hospital bed was lower than any of the hospital comparables, which ranged from 1,690 to 3,075 square feet per bed, as well as, MVS which identified 1,125 square feet as the typical size per bed for an average-grade Class A hospital. Respondent's analysis did not consider this factor which the Board found was an important distinction.

There were also some differences between the parties' analyses regarding subject's effective age and life expectancy. Respondent used an effective age of 25.1 years and a life expectancy of 45 years. By contrast, Appellant determined an effective age of 28.1 years and a life expectancy of 40 years. The result is different depreciation allowances, with Respondent concluding depreciation of 55.8% and Appellant finding 70.2%. The Board found better support for Appellant's figures. Appellant determined a life expectancy of 40 years based on three (3) separate sources of information: a hospital replacement study, MVS, and the American Hospital Association. Respondent relied on MVS and an internet posting with little to no details concerning how the 40 - 50 year hospital life was determined. The Board found adequate support for the 28.1 year effective age determined by Appellant.

In appeals to this Board, pursuant to Idaho Code § 63-511, the burden is with Appellant to establish subject's valuation is erroneous by a preponderance of the evidence. Given the evidence presented in this matter, the Board finds the burden of proof satisfied. Appellant's

value conclusion was found to represent the better supported and more thorough analysis of subject's current market value. By contrast, the Board found a number of concerns with different aspects of Respondent's sales comparison and cost approaches to value.

Based on the above, the decision of the Canyon County Board of Equalization is reversed to reflect a market value of \$13,500,000 for subject, allocated as follows.

Hospital building	\$11,399,500
Kaley building	\$ 560,000
<u>Land</u>	<u>\$ 1,540,500</u>
Total	\$13,500,000

#### FINAL ORDER

In accordance with the foregoing Final Decision, IT IS ORDERED that the value decision of the Canyon County Board of Equalization concerning the subject parcel be, and the same hereby is, REVERSED lowering subject's market valuation to \$13,500,000, as detailed above.

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 24<sup>th</sup> day of April, 2017.