BEFORE THE IDAHO BOARD OF TAX APPEALS

JACOBSON COLUMBIA, LLC, Appellant, v. ADA COUNTY, Respondent.	)))))))))))	APPEAL NOS. 18-A-1021 & 18-A-1022 FINAL DECISION AND ORDER

COMMERCIAL PROPERTY APPEALS

These appeals are taken from a decision of the Ada County Board of Equalization denying an appeal of the valuation for taxing purposes on properties described by Parcel Nos. R1525500010 and R1525500020. The appeals concern the 2018 tax year.

These matters came on for hearing November 8, 2018 in Boise, Idaho before Hearing Officer Cindy Pollock. LLC Members Blaine and Cynthia Jacobson appeared at hearing for Appellant. Chief Deputy Assessor Brad Smith represented Respondent.

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

The issue on appeal concerns the market value of two (2) adjacent commercial properties.

The decisions of the Ada County Board of Equalization are affirmed.

FINDINGS OF FACT

Parcel No. R1525500010 (Appeal No. 18-A-1021)

The assessed land value is $157,900, and the improvements' value is $254,400, totaling $412,300. Appellant agrees with the assessed land value, however, contends the value of the improvements is $204,300, totaling $362,200.

Parcel No. R1525500020 (Appeal No. 18-A-1022)

The assessed land value of this unimproved parcel is $69,200. Appellant contends the correct value is $46,200.

The subject properties are operated together as a single retail commercial enterprise. Originally, the properties were a single parcel, however, due to a shift in tax code areas, the rear unimproved parcel was split from the improved parcel. Respondent characterized the situation as an administrative split solely for purposes of taxation. As such, the parties' respective appraisal analyses considered the properties as a single economic unit. This decision will likewise consider and refer to subjects as a single property for purposes of valuation.

The subject property is located in the Columbia Marketplace shopping center in east Boise, Idaho. The shopping center is anchored by an Albertson's grocery store, with the remaining sites in the center occupied by a myriad of business types, including several different eateries. Subject, which is attached to the western side of the grocery store, is a 7,467 square foot retail space constructed in 1999. The retail space is split into three (3) suites, plus some storage space carved out of the back portion of the building.

Appellant noted subject's assessed value has increased roughly 32% since acquiring the property in 2014 for $365,000, and nearly 20% since 2016, and questioned whether the market supported such increases. Appellant was particularly concerned whether adequate consideration was given to subject's difficult performance history. It was explained subject has never been fully leased since the building was constructed in 1999, and has had nine (9) different owners during that time. Appellant reported only one (1) tenant, a quick service restaurant, has continuously occupied a suite in the building since its inception. Other portions of the building have been occupied infrequently throughout the years, with a fifteen (15) month lease beginning in late

2004, a two (2) month lease in 2012, and a six (6) week lease in late 2014. In all, Appellant calculated only 22%, or 1,619 square feet, of the building has been continuously leased, with the remaining 78% of the available space sitting vacant more than 92% of the time. As of January 1, 2018, there was only one (1) tenant leasing a suite in the building. Appellant expressed several concerns with the immediate neighborhood generally, and subject specifically. First, Appellant characterized the back vacant subject parcel as mostly unuseable. It was explained the this parcel was mostly consumed by a pedestrian right-of-way, a powerline easement, and an access easement for the neighboring grocery store. Photographs depicting use of the back parcel by delivery trucks servicing the grocery operation were provided. In Appellant's view, the back parcel has no utility for the subject building's occupants, and this allegedly was not fairly considered in the parcel's assessment.

As for the broader east Boise neighborhood, Appellant stated the area has not developed as anticipated. It was noted Boise's development has largely crept westward toward Meridian, not east. Appellant illustrated this point by offering an aerial photograph showing subject being surrounded on three (3) sides by undeveloped desert land. West Boise by contrast was shown more densely populated and developed. Appellant cited population statistics, which indicated a population of 2,100 within a one (1) mile radius of subject, and an annual growth rate in the neighborhood of 1.79%. These figures were noted to lag behind Idaho's overall growth rate of 4% and Ada County's growth rate of more than 7%. It was further noted the local population is largely employed in the manufacturing sector, with the primary employer being Micron located less than two (2) miles from subject. Appellant explained because Micron has an expansive campus with numerous on-site dining options for the company's employees, few workers venture off campus in search of food.

Appellant next focused on some of subject's physical issues believed to contribute to the property's poor leasing history. One (1) issue articulated was the depth of the building, which at 100 feet, was argued to be excessive for small retail-type businesses. It was judged a depth of fifty (50) to sixty (60) feet would be ideal for the type of tenants which would potentially lease space in the subject building. On this point, Appellant explained a prior owner had partitioned off a section in the rear of the building in an attempt to attract tenants to lease a more appropriately sized suite. This back portion, representing 1,668 square feet, or nearly 23% of the total area, is used by the restaurant tenant to store business records. No rent or other fees are charged for the tenant's use of the space. In fact, pursuant to the master covenants, the storage space cannot be leased to anyone. As this space cannot earn income, Appellant contended it contributes little or no value to subject.

In addition to preventing the lease of subject's storage space, the master covenants also restrict the type of tenant allowed to lease space in the subject building. Appellant counted more than forty (40) prohibited business types. A small sampling of prohibited types includes a warehouse, a bakery, a bar or tavern, a health spa, an automotive business, a skating rink, a medical office, a dance hall, an educational enterprise, a video arcade, and an entertainment business. Such restrictions were argued to negatively impact subject's relative competitiveness in the marketplace.

Turning to the matter of subject's valuation, Appellant developed a couple different value estimates under the income approach. Using Respondent's income approach as a basic template, Appellant changed the income and expense inputs to reflect subject's actual performance. In the first model, subject's actual lease income was used for the potential gross income estimate, which was noted to be approximately one-half (½) the potential gross income used in Respondent's income approach. In similar fashion, subject's actual operating expenses were utilized to derive the net operating income, which was then capitalized at 7.75%. The result was a value estimate of $32,606.

In an alternative approach, Appellant increased subject's potential gross income by including the lease income expected from a tenant who leased a suite beginning in April 2018. Including this income increased subject's potential gross income by nearly $13,000. The same expense figures and capitalization rate from the above model were applied against the income, resulting in a value indication of $130,542.

Lastly, Appellant contended subject was inequitably assessed compared to other properties situated in the shopping center. Assessment information concerning seven (7) properties in the shopping center was offered. The summary chart revealed a range of change in assessed land values for the referenced parcels compared to the prior year, ranging from -4.2% to +14.2%. Subject's land value increased 25.6%, which in Appellant's view suggested inequitable assessment between subject and other parcels in the shopping center.

Respondent spoke first to the perceived inequitable assessment of subject. It was explained subject was physically reappraised for the 2018 assessment year. Respondent clarified the reappraisal effort did not focus on a specific geographic area, such as the entire shopping center, but rather on a particular category of commercial property throughout the county; specifically, anchored retail properties. So while the raw assessment data provided by Appellants did show varying rates of value change, the bulk of the properties referenced were not part of the reappraisal campaign and therefore received different value changes on a percentage basis for 2018.

In support of subject's assessment, Respondent relied primarily on the income approach. In considering the subject improvements, Respondent identified 5,850 of the building's total 7,464 square feet as leasable retail space. The remaining portion was characterized as warehouse storage. Rather than relying on subject's actual income, Respondent's model sought to develop an estimate of the potential income using market-based lease rates. A blended rate of $8 per square foot was used, which was noted to be below current lease rate levels according to current listings from the immediate shopping center. This lesser rate was used in an attempt to account for Appellant's inability to lease subject's storage space. It was also remarked the $8 per square foot lease rate was notably less than the $16.33 per square foot rate currently paid by the long-term tenant who was the only tenant of the building as of January 1, 2018. To this, Respondent added 3% as a potential gross income trend, and a vacancy factor of 10%. Respondent acknowledged subject's vacancy has never been as low as 10%. It maintained however, the use of the 10% rate was proper because it represented typical vacancy in the marketplace.

Respondent stressed the importance of using market-derived inputs in the income approach to ensure equitable assessment across a particular commercial property type. An expense rate of 32% was applied against the potential operating income estimate. Respondent noted market expense rates varied between 5% and 7%, however, explained a higher expense rate was used in subject's valuation in an attempt to recognize subject's history of financial under-performance. A capitalization rate of 7.75% was utilized, which yielded a value estimate of $481,510.

Respondent also provided information concerning three (3) commercial sales. Sale No. 1, located in Meridian, was a non-anchored 6,500 square foot commercial building constructed in 2005. The property sold in March 2016 for $655,000, or $100.77 per square foot. Sale No. 2 concerned a 4,256 square foot retail building constructed in 1986. This unanchored property, located in the Boise Bench neighborhood, sold in April 2017 for $378,500, or $88.93 per square foot. Lastly, Sale No. 3 closed in August 2016 for $1,060,000, or $145.42 per square foot. Located in Eagle and anchored by two (2) big box stores, the property consisted of a 7,289 square foot retail building constructed in 2005. Based on the per-square-foot price range indicated by the sales, Respondent concluded subject's assessed value rate of $64.48 per square foot was reasonable.

Lastly, Respondent offered some current vacant retail listings from subject's immediate neighborhood. Ten (10) such listings were included, with asking prices ranging from $196,485 to $541,737, or from $3.25 to $14.00 per square foot. With an assessed land value of $5.50 per square foot, Respondent noted subject's valuation represented the lower end of the range indicated by current listings in the area.

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 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, 2018 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 three (3) primary methods for determining market value include the sales comparison approach, the income approach, and the cost approach. *Merris v. Ada Cnty.*, 100 Idaho 59, 63, 593 P.2d 394, 398 (1979). The parties primarily relied on the income approach to develop their respective value positions, which approach is commonly used to estimate the value of income-producing property.

Before the issue of subject's market value, we will first address Appellant's concerns with the unleasable storage space in the rear of the building. Appellant contended the space is essentially waste because the master covenants prevent it from being leased. While we agree the storage space contributes nothing in the form of direct revenue generation, it does nonetheless have some value. The space exists and is actually used, albeit for the limited purpose of storing business records for the restaurant tenant at no charge. Such limited use should certainly be reflected in the rate used to determine the contributory value of the space. Though the rate used in the assessment was not apparent in the record, Respondent reported the storage space was valued well below the rate used for the leasable retail suites. In other words, Respondent recognized the limited utility of the storage space and valued it accordingly. Without more evidence indicating a lower value for the storage space, the Board did not find sufficient cause to adjust subject's assessment for this factor.

Turning more squarely to subject's market value, the Board would like to acknowledge the efforts of both parties in providing relevant evidence. While these efforts were appreciated, there were some concerns with aspects of the parties' analyses. Regarding Appellant's income approach models, our primary concern was the use of subject's actual revenue and expense figures throughout. Typically, the income approach, as well as the other approaches to value, are developed using market-derived inputs and adjustments. Said differently, the estimation of market value requires the use of market rent. For assessment purposes this is done to minimize potential inequitable assessments across property types. If an individual property's income and expense numbers are used there is an increased likelihood of "rewarding" an under-performing property, which may be plagued with poor management or some other factor, by assessing the property lower than its peers. On the flip side, using actual revenues and expenses could "punish" a well-performing property by assessing it higher than other similar properties. That being said, it is still imperative to consider, in fee simple, the potential value-impacting factors unique to a particular property being valued. See IDAPA 35.01.03.217.

In the case at bar, a unique factor associated with subject is its historically high vacancy rate, which has persisted for many years. On this point, it is important to note the high vacancy impacts the operating expenses paid by the landlord. Some of this expense would normally be the responsibility of the tenants if the building were more fully leased. It is not clear what exactly causes subject's high rate of vacancy. Based on the information provided, it is likely multiple factors have contributed. In this particular circumstance, the Board finds some special consideration for the increased operating expenses is warranted.

There is another notable concern with a strict reliance on subject's actual revenue and expense figures. Because the only revenue generated is from the single present tenant, this income approach effectively attributes zero value to the remaining unleased suites. Similar to what was noted before with respect to the storage space, the unleased retail space does indeed exist, is well maintained, and is found to have the potential for future income generation. As such, the unleased suites must be valued, even if at a different rate than the leased space. Appellant’s income approach model failed to attribute a reasonable potential revenue to the unleased suites, which in the Board’s view was a fatal flaw in the analysis.

Respondent’s income approach, where the inputs and adjustments were more closely representative of the market, was better received by the Board. Though several of the inputs in Respondent’s model were at full market levels, the potential gross income, at $8 per square foot, was noted to be below current asking prices within subject’s shopping center and the immediate neighborhood. These lease comparables were shown to range between roughly $10 and $12 per square foot. The 32% operating expense rate was also notably higher than the typical expense rate, which Respondent reported ranged from 5% to 7%. These more favorable revenue and expense rates were used in an attempt to recognize subject’s well-documented and long-running performance deficiencies, which appear to have been caused by factors such as the restrictive covenants and excessive building depth. Respondent’s special consideration of subject’s unique situation was found to be reasonable and appropriate in this case.

Respondent’s sales comparison approach was relatively less reliable in the Board's judgment. Though the sale properties were generally representative of subject in terms of size and quality, there appeared to be few other similarities. All the sale properties were located in more developed and densely populated areas in and near west Boise. The traffic counts for these sale properties were noted by Appellant to far exceed subject's traffic count. Curiously, no location adjustments were made. Indeed, no adjustments were attempted in comparing to the subject. Rather, Respondent simply reported the respective sale price rates and stated subject's value was reasonable in comparison. The Board would have been interested in a more traditional analysis with adjustments made for key value factor differences. Accordingly, we held only minimal weight should be given Respondent's sales comparison approach.

Pursuant to Idaho Code § 63-511, the burden is Appellant's to establish subject's valuation is erroneous by a preponderance of the evidence. Given the record in this case, we did not find the burden of proof satisfied. Appellant thoroughly detailed factors argued to contribute to subject's difficult performance history, however, failed to correlate such factors to quantifiable and appropriate appraisal inputs or adjustments. Respondent, on the other hand, endeavored to recognize subject's deficiencies in its analysis by using a below-market blended lease rate to calculate potential gross income. Respondent also applied a higher operating expense rate. Certainly Respondent could have chosen to adjust different inputs in the model, such as the vacancy rate instead of the expense rate, but we found no obvious or clear error in the judgments used in this case. "[T]he question is not what someone else, however eminent he may be in the field of appraisal . . . may think is the proper method, but involves simply the determination as to whether the method used by the assessor was legitimate and fair, and was a reasonable method to use in arriving at the value of the property in question." *Abbot v. State Tax Comm'n.*, 88 Idaho 200, 206, 398 P.2d 221, 224 (1965). In this particular case, we found Respondent's value conclusion more indicative of subject's current market value.

Given the above, the value decisions of the Ada County Board of Equalization are affirmed.

FINAL ORDER

In accordance with the foregoing Final Decision, IT IS ORDERED that the decisions of the Ada County Board of Equalization concerning the subject parcels be, and the same hereby are, AFFIRMED.

DATED this 27th day of February, 2019.