

07-0172
LOCALLY ASSESSED PROPERTY
TAX YEAR: 2006
SIGNED 11-04-08
COMMISSIONERS: P. HENDRICKSON, M. JOHNSON, D. DIXON
EXCUSED: R. JOHNSON
GUIDING DECISION

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER, Petitioner, v. BOARD OF EQUALIZATION OF DAVIS COUNTY, STATE OF UTAH, Respondent.	FINDINGS OF FACT, CONCLUSIONS OF LAW, AND FINAL DECISION Appeal No. 07-0172 Parcel No. ##### Tax Type: Property Tax / Locally Assessed Tax Year: 2006 Judge: Chapman
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This Order may contain confidential "commercial information" within the meaning of Utah Code Ann. §59-1-404, and is subject to disclosure restrictions as set out in that section and regulation pursuant to Utah Admin. Rule R861-1A-37. The rule prohibits the parties from disclosing commercial information obtained from the opposing party to nonparties, outside of the hearing process. However, pursuant to Utah Admin. Rule R861-1A-37, the Tax Commission may publish this decision, in its entirety, unless the property taxpayer responds in writing to the Commission, within 30 days of this notice, specifying the commercial information that the taxpayer wants protected. The taxpayer must mail the response to the address listed near the end of this decision.

Presiding:

Pam Hendrickson, Commission Chair
Kerry R. Chapman, Administrative Law Judge

Appearances:

For Petitioner: PETITIONER REP 1, Attorney
 PETITIONER REP 2, MAI
For Respondent: RESPONDENT REP 1, Deputy Davis County Attorney
 RESPONDENT REP 2, Davis County Assessor
 RESPONDENT REP 3, Appraiser, Davis County Assessor's Office

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for a Formal Hearing on October 28, 2008. Based upon the evidence and testimony presented at the hearing, the Tax Commission hereby makes

its:

FINDINGS OF FACT

1. The tax at issue is property tax.
2. The lien date at issue is January 1, 2006.
3. The subject property is identified as Parcel No. ##### and is located at ADDRESS in CITY, Davis County, Utah.
4. For the 2006 tax year, the subject property was originally assessed at \$\$\$\$\$, which the Davis County Board of Equalization (“County BOE”) reduced to \$\$\$\$\$.
5. The property owner asks the Commission to reduce the subject’s fair market value to \$\$\$\$\$.
6. The County asks the Commission to increase the subject’s fair market value to \$\$\$\$\$, the value originally assessed by the County Assessor for the subject year.
7. The subject property is comprised of 2.53 acres of land and a relatively large, single-tenant retail store that is 37,767 square feet in size. The 37,767 square feet of total space includes 3,825 square feet of mezzanine space.
8. The subject property is located in a major shopping area of Davis County. The subject is accessed from STREET, but it is located behind other buildings that front STREET. Access to the subject is through shared driveways and parking areas. Additionally, this property is located near both a COMPANY A and COMPANY B.
9. The subject property was built in 1994 and was used as a COMPANY C store until that chain closed and vacated the property in early 2005. The store has remained vacant since that time,

including the lien date at issue. The front facade of the subject building is typical to the COMPANY C chain and would probably need remodeling to attract most tenants.

10. For the past four years, the property owner has offered to lease the store for \$\$\$\$ per square foot. The property owner explained that this list price is a “starting point” for negotiations. The property owner has engaged in significant negotiations with two potential tenants, specifically COMPANY D and COMPANY E. COMPANY D only wanted to lease a portion of the property, which would have required extensive tenant improvements to divide the current single-tenant store into multi-tenant space. COMPANY E wanted the property owners to significantly increase the size of the building, which would have also required extensive tenant improvements. Both potential tenants eventually chose not to lease the subject property.

County’s Information and Arguments

11. The County explained that its policy is to assess all income-producing property as though it is leased, including property that is vacant on the lien date. Furthermore, the County explained that the “leased” value that it derives for a vacant property is not adjusted for any possible short-term losses that it may experience due to its vacant state.

12. The County submitted an appraisal prepared by RESPONDENT REP 3, a certified general appraiser who works in the County Assessor’s Office. Exhibit R-1. RESPONDENT REP 3 testified on behalf of the County.

13. The County’s appraisal was prepared in accordance with its policy as explained above; i.e., RESPONDENT REP 3 estimated the subject property’s value as though it was leased, without determining whether the vacant subject would experience any short-term losses or extraordinary expenses that might affect its value as of the lien date.

14. In his appraisal, RESPONDENT REP 3 determined that the subject property had a value of \$\$\$\$\$ as of the lien date. RESPONDENT REP 3 estimated the subject's value at \$\$\$\$\$ using the cost approach and at \$\$\$\$\$ using the income approach. In reconciling these values, he gave considerable weight to the income approach and estimated a final value of \$\$\$\$\$ for the subject property.

15. In his cost approach, RESPONDENT REP 3 determined the land value through a market approach and the improvements value through "Marshall Valuation Cost" information. With these methods, he determined a total cost value of \$\$\$\$\$. However, with its cost approach, the County has determined the value of a property that was built to the unique specifications of a national-credit tenant, specifically COMPANY C. The County, however, has not analyzed whether there should be a deduction for economic or functional obsolescence to recognize that the tenant for which the building was constructed has vacated the property as of the lien date. Because a large vacant store such as the subject would require substantial tenant improvements before leasing to a similar, national-credit tenant or, without improvements, would rent to a significantly lower quality tenant, the Commission does not find the County's cost approach convincing.

16. For his income approach, RESPONDENT REP 3 determined a "stabilized" lease rate, vacancy rate, and expense rate to estimate "stabilized" net operating income, then applied a capitalization rate to derive a value of \$\$\$\$\$ for the subject property. RESPONDENT REP 3 derived his lease rate from comparable leases in CITY. However, he derived his vacancy rate from county-wide information from all retail space in Davis County, not just large, single-tenant stores. Furthermore, he determined his capitalization rate from all retail space in COUNTY 1.

17. RESPONDENT REP 3 determined a lease rate of \$\$\$\$\$ per square foot for the subject property based on seven comparables located near the subject property. One of the comparables was

the subject itself, which is listed for \$\$\$\$ per square foot. However, as explained earlier, the property owner explained that his is a starting point for negotiations with potential tenants. There is no indication that the subject property would lease for \$\$\$\$ per square foot without substantial tenant improvements. Because the County did not make adjustments for such tenant improvements, the Commission does not consider the \$\$\$\$ per square foot asking price relevant.

18. The remaining six lease comparables are for properties leased to national-credit tenants and show a wide variety of lease rates, from \$\$\$\$ to \$\$\$\$ per square foot. Some of these leases concern properties vacated by the original tenant, but leased to other national-credit tenants after tenant improvements were made. The County, however, did not know the extent or cost of the tenant improvements that were required before the current national-credit tenant agreed to the lease rates the County used as comparables. However, the County was aware that Comparable #5 was vacant for a year after its original tenant left, before being leased to COMPANY F for \$\$\$\$ per square foot.

19. RESPONDENT REP 3 admitted that the \$\$\$\$ lease rate that the property owner is asking for the subject property is too high. He determined that the market lease rate of the subject property would be \$\$\$\$ per square foot, based on the lease rates of properties leased to national-credit tenants after tenant improvements were made to attract those tenants. Such comparables do not appear similar to the subject property in its vacant, “as-is” condition on the lien date. It is improbable that another national-credit tenant would lease the subject property without substantial tenant improvement. Without an adjustment to account for these improvements, the Commission does not find the County’s lease analysis to be convincing. If such an adjustment were made, it is likely that the lease rate for the subject, in its “as-is” condition on the lien date, would be below \$\$\$\$ per square foot.

Property Owner’s Information and Arguments

20. PETITIONER REP 2, MAI, testified on behalf of the property owner. He explains that as of the lien date, the subject property was a relatively large, single-tenant store that had recently lost its first-generation, national-credit tenant, specifically COMPANY C. PETITIONER REP 2 further contends that properties such as the subject, which are built to the specifications of a national tenant, need significant modifications, or tenant improvements, before they can be rented to a similar type of tenant. He explains that the cost of tenant improvements needed to attract to a second-generation tenant that is not a national-credit tenant range between \$\$\$\$ and \$\$\$\$ per square foot. He also indicates that the cost of tenant improvements needed to attract another national-credit tenant could equal or exceed \$\$\$\$ per square foot.

21. PETITIONER REP 2 also explains that a large vacant store will experience short-term rent losses during its lease-up period, as well as atypical expense costs and leasing costs not considered in a “stabilized” income approach. For these reasons, he believes that as of the lien date, a buyer would pay less for the vacant subject property than it would have paid had it been occupied on this date.

22. PETITIONER REP 2 used two different scenarios with which to estimate the subject’s value as of the lien date. The first scenario is to value the property in its “as-is” state on the lien date; i.e., without the property owner having to expend any significant tenant improvements. For this scenario, the property owner submitted an appraisal by PETITIONER REP 2. Exhibit P-1. Without significant tenant improvements, PETITIONER REP 2 contends that the property would not attract a mid-quality or high-quality tenant, but would instead lease to a lower-quality tenant. In his appraisal, he derived a value of \$\$\$\$ using the market approach and a value of \$\$\$\$ using the income approach. In reconciling these values, PETITIONER REP 2 determined that the income approach should receive the greater weight and determined a final value of \$\$\$\$ for the subject property.

23. In the second scenario, PETITIONER REP 2 determined the amount of the short-term losses and costs that the property owner would incur if it leased the subject to a mid-quality tenant after moderate tenant improvements of \$\$\$\$ per square foot. Exhibit P-2. He determined that the losses and costs for a two-year lease-up period would total approximately \$\$\$\$ and that the losses and costs for a one-year lease-up period would total approximately \$\$\$\$\$. These amounts appear reasonable and were not contested as being excessive by the County. The County's appraisal, which estimates the subject's value at \$\$\$\$\$, appears to estimate the subject's value as though tenant improvements have already been made and that the subject would lease to a mid-quality to high-quality tenant. The Commission notes that the COMPANY F comparable in the County's appraisal was vacant for a year before it leased. If PETITIONER REP 2's estimated losses and costs of \$\$\$\$ for a one-year lease-up period are deducted from the County appraisal's value of \$\$\$\$\$, a final value of \$\$\$\$ is derived.

24. In his appraisal's market approach, PETITIONER REP 2 compared the subject to four other relatively large stores, three of which were vacant at the time of sale. The fourth had been converted to accommodate multiple tenants. One of the comparables was located in CITY, while the others were located in other cities in Davis County. PETITIONER REP 2 explains that he used comparables throughout Davis County because the Wasatch Front is a regional market for these types of buildings. This does not appear unreasonable, as the County used county-wide information not only from Davis County but also Salt Lake County in its income approach. All of the comparables were either second or third-generation buildings at the time of sale, meaning that they sold after their original tenants had vacated them. Two of the comparables had had first-generation, national-credit tenants prior to their sales. For example, Comparable #2's original tenant had been Company G, and Comparable #3's original tenant had been Company H. These comparables sold for prices per square foot that ranged between \$\$\$\$ and \$\$\$\$\$. PETITIONER REP 2 adjusted the comparables

to prices that ranged between from \$\$\$\$ and \$\$\$ per square foot. From this information, he estimated the subject's value at \$\$\$ per square foot. When the \$\$\$ price is applied to subject's main floor space alone (i.e., not to the mezzanine), a market value of approximately \$\$\$ is derived. If this rate is also applied to the mezzanine space, a total market value of approximately \$\$\$ is derived. The Commission finds that PETITIONER REP 2 has used comparables in his market approach that are affected by circumstances similar to those that affect the subject property as of the lien date. As a result, the Commission finds PETITIONER REP 2's market approach to appear reasonable.

25. In his appraisal's income approach, PETITIONER REP 2 compared the subject to three other relatively large stores that had been leased to second or third-generation tenants between October 2003 and January 2006. These three stores are similar to the subject in that they, like the subject, had lost their first-generation tenants. These stores leased for rates ranging between \$\$\$ and \$\$\$ per square foot. PETITIONER REP 2 also provided a fourth comparable that showed the rental rate paid by a first-generation tenant for a newly-built store. This tenant, specifically COMPANY I, leased the new property for \$\$\$ per square foot in May 2005. Using these comparables, PETITIONER REP 2 estimated that the subject would rent for \$\$\$ per square foot in its "as-is" condition; i.e., without any tenant improvements. PETITIONER REP 2's evidence suggests that without significant tenant improvements being made, relatively large retail stores rent at lower rates and to lesser-quality tenants after they are vacated by their first-generation, national-credit tenants. As a result, PETITIONER REP 2's estimated lease rate of \$\$\$ per square foot for the subject in its "as-is" condition does not appear unreasonable, based on the totality of both parties' evidence.

APPLICABLE LAW

1. Utah Code Ann. §59-2-103(1) provides that “[a]ll tangible taxable property shall be assessed and taxed at a uniform and equal rate on the basis of its fair market value, as valued on January 1, unless otherwise provide by law.”

2. For property tax purposes, “fair market value” is defined in UCA §59-2-102(12) to mean:

the amount at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of the relevant facts. For purposes of taxation, “fair market value” shall be determined using the current zoning laws applicable to the property in question. . . .

3. UCA §59-2-1006 provides that a person may appeal a decision of a county board of equalization to the Tax Commission, pertinent parts as follows:

(1) Any person dissatisfied with the decision of the county board of equalization concerning the assessment and equalization of any property . . . may appeal that decision to the commission. . . .

. . . .

(3) In reviewing the county board's decision, the Commission may:

- (a) admit additional evidence;
- (b) issue orders that it considers to be just and proper; and
- (c) make any correction or change in the assessment or order of the county board of equalization.

(4) In reviewing the county board's decision, the commission shall adjust property valuations to reflect a value equalized with the assessed value of other comparable properties if:

- (a) the issue of equalization of property values is raised; and
- (b) the commission determines that the property that is the subject of the appeal deviates in value plus or minus 5% from the assessed value of comparable properties.

. . . .

4. Any party requesting a value different from the value established by the county board of equalization has the burden to establish that the market value of the subject property is other than the value

determined by the county board of equalization. To prevail, a party must: 1) demonstrate that the value established by the county board of equalization contains error; and 2) provide the Commission with a sound evidentiary basis for changing the value established by the county board of equalization to the amount proposed by the party. *See Nelson v. Bd. Of Equalization of Salt Lake County*, 943 P.2d 1354 (Utah 1997); *Utah Power & Light Co. v. Utah State Tax Commission*, 530 P.2d. 332 (Utah 1979).

CONCLUSIONS OF LAW

1. The Commission finds that the County's appraisal does not adequately address the subject's vacant, "as-is" condition on the lien date. The appraisal appears to value the subject as though it has already been remodeled to accommodate a new mid-quality to high-quality tenant. The Commission finds PETITIONER REP 2's testimony about relatively large, vacant retail stores and the costs incurred to lease them to new mid-quality and high-quality tenants to be convincing. The Commission recognizes that the County may have a policy not to recognize such factors and costs in its appraisal process. However, such a practice tends, as in this case, to overestimate a property's fair market value.

2. Based on the totality of the testimony and the evidence submitted by both parties, the Commission finds that the County has not demonstrated that the subject's fair market value as of the lien date is \$\$\$\$\$, as established by the County BOE, or higher. Instead, the Commission finds that the property owner has shown that the current value is incorrect and that \$\$\$\$\$ is a reasonable value for the subject in its current, "as-is" condition on the lien date.

DECISION AND ORDER

Based upon the foregoing, the Tax Commission finds that the subject property's value of \$\$\$\$\$, as established by the County BOE, should be reduced to \$\$\$\$\$. The Davis County Auditor is ordered to adjust its records in accordance with this decision. It is so ordered.

Appeal No. 07-0172

DATED this _____ day of _____, 2008.

Kerry R. Chapman
Administrative Law Judge

BY ORDER OF THE UTAH STATE TAX COMMISSION:

The Commission has reviewed this case and the undersigned concur in this decision.

DATED this _____ day of _____, 2008.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

Marc B. Johnson
Commissioner

D'Arcy Dixon Pignanelli
Commissioner

Notice of Appeal Rights: You have twenty (20) days after the date of this order to file a Request for Reconsideration with the Tax Commission Appeals Unit pursuant to Utah Code Ann. §63-46b-13. A Request for Reconsideration must allege newly discovered evidence or a mistake of law or fact. If you do not file a Request for Reconsideration with the Commission, this order constitutes final agency action. You have thirty (30) days after the date of this order to pursue judicial review of this order in accordance with Utah Code Ann. §59-1-601 et seq. and §63-46b-13 et seq.

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