

08-2739
LOCALLY ASSESSED PROPERTY
SIGNED 06-29-09

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER,

Petitioner,

v.

BOARD OF EQUALIZATION OF
SALT LAKE COUNTY, STATE OF UTAH,

Respondent.

INITIAL HEARING ORDER

Appeal No. 08-2739

Parcel No. #####

Tax Type: Property Tax / Locally Assessed

Tax Year: 2008

Judge: Chapman

This Order may contain confidential "commercial information" within the meaning of Utah Code Sec. 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:

Kerry R. Chapman, Administrative Law Judge

Appearances:

For Petitioner: PETITIONER REP 1, Representative
PETITIONER REP 2, Property Owner

For Respondent: RESPONDENT REP from the Salt Lake County Assessor's Office

STATEMENT OF THE CASE

This matter came before the Commission for an Initial Hearing pursuant to the provisions of Utah Code Ann. §59-1-502.5, on June 22, 2009.

At issue is the fair market value of the subject property as of January 1, 2008. The subject property is a 17-unit apartment building located at ADDRESS in CITY, Utah. For the 2008 tax year, the property was originally assessed at \$\$\$\$\$, which the Salt Lake County Board of Equalization ("County BOE") reduced to \$\$\$\$\$. On the petition the property owner submitted to the Commission, he asked that the subject

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property's value be further reduced to \$\$\$\$\$. The County asks the Commission to further reduce the subject's value to \$\$\$\$\$.

APPLICABLE LAW

Utah Code Ann. §59-2-1006(1) provides that “[a]ny person dissatisfied with the decision of the county board of equalization concerning the assessment and equalization of any property, or the determination of any exemption in which the person has an interest, may appeal that decision to the commission”

Any party requesting a value different from the value established by the County BOE 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.

For a party who is requesting a value that is different from that determined by the County BOE to prevail, that party must (1) demonstrate that the value established by the County BOE contained error, and (2) provide the Commission with a sound evidentiary basis for reducing the value established by the County BOE to the amount proposed by the party. *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).

DISCUSSION

The subject property is known as (X) and is comprised of 0.37 acres of land and a 17-unit apartment building. The 3-story apartment building was built in 1965 and is 13,550 square feet in size. The building consists of 6 one-bedroom units, 10 two-bedroom units and 1 three-bedroom unit.

In his petition, the property owner asserts that the subject was assessed at \$\$\$\$\$ for the 2007 tax year and that a reasonable increase of 8.5% would result in a value of \$\$\$\$\$ for the subject for the 2008 tax year. The property owner also provided income approach information and asserts that an income approach will show a value around \$\$\$\$\$ to be reasonable.

For the County, RESPONDENT REP produced an income approach with which she estimated the subject's value to be \$\$\$\$\$. She also prepared a market approach with which she estimated the value to be \$\$\$\$\$. She reconciled the two values and derived a final estimate of value in the amount of \$\$\$\$\$. She asks the Commission to reduce the subject's value to \$\$\$\$\$ based on this information.

Income Approach. The parties disagree on many of the components that comprise an income approach to value. The Commission will separately address the various components in dispute, specifically: 1) potential gross income; 2) reserves expense; 3) operating expenses; and 4) capitalization rate.

Potential Gross Income ("PGI"). The property owner proffered a December 2007 rent roll, which shows that: 1) the 1 three-bedroom unit was leased for \$\$\$\$\$ per month; 2) the 10 two-bedroom units were leased at rates ranging between \$\$\$\$\$ and \$\$\$\$\$ per month; and 3) five of the one-bedroom units were leased for rates of \$\$\$\$\$ and \$\$\$\$\$ per month. One of the one-bedroom units did not generate revenue, as it is occupied rent-free by the apartment managers in return for their management services.

In developing the County's PGI for the property, RESPONDENT REP determined that the three-bedroom unit would lease for \$\$\$\$\$ per month, the two-bedroom units would lease for \$\$\$\$\$ per month and the one-bedroom units, including the one occupied by the managers, would lease for \$\$\$\$\$ per month. RESPONDENT REP acknowledged that many of the units were actually leased at lower rates. However, she determined that the highest lease rates represent "market" rents as of the lien date because the leases entered into nearest to the lien date were at the higher amounts. With this approach, RESPONDENT REP determined a PGI of \$\$\$\$\$.

Many of the actual lease rates were established more than two years ago. The property owner argues that these older lease rates should also be considered in establishing PGI. The Commission, however, believes that older lease rates that are appreciably lower than lease rates entered into near the lien date should generally be adjusted for purposes of an income approach used to establish value as of the lien date. Based on

the lease rates received during the entirety of 2007, the Commission will use the following rates to establish PGI, specifically: 1) \$\$\$\$ per month for the 1 three-bedroom unit; 2) \$\$\$\$ for the 10 two-bedroom units; and 3) \$\$\$\$ per month for 5 of the one-bedroom units that are rented. The Commission does not include any rent for the unit that is occupied by managers rent-free. Based on these rents, the Commission arrives at a PGI of \$\$\$\$.

After adjusting PGI by a vacancy rate of 10% and adding \$\$\$\$ of additional laundry income, the Commission arrives at an effective gross income (“EGI”) of \$\$\$\$.

Reserves Expense. In her income approach, RESPONDENT REP deducted a reserves expense equal to 3% of EGI, explaining that it was the County’s policy to use this rate. The property owner countered that an apartment building nearly 50 years old, such as the subject property, would need reserves far in excess of 3% and that he usually uses 10% for buildings this old. RESPONDENT REP stated that she had no argument against the property owner’s position that a 3% reserves rate was too low for the subject property. However, she stated that she could not recommend a rate that differed from County policy of 3%. The Commission believes that a 10% reserves rate may be a bit high. However, based on the information provided at the Initial Hearing, the Commission will use a 10% reserves expense rate in the income approach.

Operating Expenses. The property owner proffered evidence that the subject’s operating expenses were \$\$\$\$ for the 2007 tax year (after property taxes were deducted). In her income approach, RESPONDENT REP deducted operating expenses of \$\$\$\$, stating that she was under the impression she has used actual expenses. However, RESPONDENT REP deducted “management fees” that did not appear on the property owner’s expense report. The Commission believes that it should not include the County’s management fee in operating expenses as it does not appear to be an actual expense and because it is roughly equivalent to the loss rent resulting from allowing the managers to live in one of the units rent-free. Based on this information, the Commission deducts \$\$\$\$ as operating expenses.

After deducting a 10% reserves expense and \$\$\$\$\$ in operating expenses from EGI, the Commission arrives at net operating income (“NOI”) of \$\$\$\$\$. Although the property owners assert that an NOI of this amount is inappropriate because NOIs for several years prior to 2007 were lower, the Commission notes that rental income appears to have increased significantly in 2007 and 2008. If vacancy in excess of “stabilized” vacancy existed in prior years, such vacancy should not be used in an income approach without adjustments. Otherwise, the temporary vacancy losses are considered to exist in perpetuity, resulting in a value that is too low.

Capitalization Rate. The County recommends a capitalization rate of %%% (prior to loading in the property tax rate), while the property owner recommends a rate of %%%. The County’s %%% rate is the median of ten capitalization rates from apartment buildings that sold between 2006 and 2008. The property owner’s %%% rate is the average of four capitalization rates from apartment buildings that sold in 2007 and early 2008. Of the County’s ten comparables, the Commission notes that the two apartment buildings built in the 1960s, like the subject, that sold in 2007 had capitalization rates of %%% and %%%, respectively. The Commission also notes that of the property owner’s comparables, two of the apartment buildings are in “average” condition, while the remaining ones are in “above average” or “good” condition. The ones in “average” condition appear most similar in condition to the subject, given the information provided at the hearing. The two “average” comparables show capitalization rates of 6.87% and 7.35%, respectively. The four comparables that appear most like the subject have capitalization rates that range between 6.5% and 7.4%. Based on these comparables, the Commission finds that the property owner’s recommended capitalization rate of 6.94% appears more reasonable than the County’s recommended rate of 6.5%.

When the effective tax rate of 0.634% is added to the 6.94% capitalization rate, an overall capitalization rate of 7.574% is derived. When the NOI of \$\$\$\$\$ is divided by this overall rate, a value of

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approximately \$\$\$\$\$ is derived for the subject property. This value equates to approximately \$\$\$\$\$ per unit for the subject's 17 units.

Earlier, the Commission expressed concern whether the reserves expense rate of 10% was too high. If a 6% reserves expense rate were used in the above income approach, the subject's NOI would be \$\$\$\$\$, which when capitalized at %%%%% results in a value of approximately \$\$\$\$\$. This value equates to approximately \$\$\$\$\$ per unit.

Sales Comparison Approach. RESPONDENT REP used six comparable sales of apartment buildings in the County's sales comparison approach. The comparables sold for values ranging between \$\$\$\$\$ and \$\$\$\$\$. Each of the comparables had between 12 and 24 units. RESPONDENT REP compared the comparables to the subject on a unit basis, a square foot basis and a room basis. With her sales comparison approach, RESPONDENT REP estimated the subject's value to be \$\$\$\$\$.

The Commission notes that two of the comparables, which are located in the "(AREA)" area of CITY, appear to have sold at prices per square foot that are significantly higher than the prices at which the other four comparables sold. If the four remaining comparables (i.e., those not in the AREA are considered, the Commission notes that they sold at prices ranging between \$\$\$\$\$ and \$\$\$\$\$ per unit. RESPONDENT REP adjusted these four comparables to adjusted prices ranging between \$\$\$\$\$ and \$\$\$\$\$ per unit. The average of these four adjusted prices is \$\$\$\$\$ per unit, which if applied to the subject's 17 units results in a value of \$\$\$\$\$ for the subject property.

RESPONDENT REP adjusted the same four comparables to prices that ranged between \$\$\$\$\$ and \$\$\$\$\$ per square foot. The average of these adjusted prices per square foot is \$\$\$\$\$, which if applied to the subject's 13,550 square feet results in a value of \$\$\$\$\$ for the subject property.

The property owner submitted five comparables that sold between \$\$\$\$\$ and \$\$\$\$\$ per unit. The comparable that sold for \$\$\$\$\$ per unit has 17 units, like the subject, and sold for a total price of \$\$\$\$\$.

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It is the only comparable that appears, like the subject, to be three stories in height. All of the other comparables appear to be two stories in height. This comparable is also in “average” condition, like the subject. The Commission notes that no other comparable sold for less than the \$\$\$\$ per unit price at which this comparable sold.

As a result, the Commission finds that the subject’s prices should be no less than \$\$\$\$ per unit, which equates to \$\$\$\$\$. The Commission notes that the \$\$\$\$ value falls within the range of values shown by the income approach, as described earlier, and RESPONDENT REP’s adjusted values for the County’s four comparables not located in the AREA. Based on this information, the Commission finds that \$\$\$\$ is a reasonable value for the subject property as of the lien date and reduces the subject’s value to this amount.

DECISION AND ORDER

Based upon the foregoing, the Tax Commission finds that the fair market value of the subject property should be reduced from \$\$\$\$, as established by the County BOE, to \$\$\$\$ for the 2008 tax year. The Salt Lake County Auditor is ordered to adjust its records in accordance with this decision. It is so ordered.

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall be mailed to the address listed below and must include the Petitioner's name, address, and appeal number:

Utah State Tax Commission
Appeals Division
210 North 1950 West
Salt Lake City, Utah 84134

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Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this _____ day of _____, 2009.

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 _____, 2009.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

Marc B. Johnson
Commissioner

D'Arcy Dixon Pignanelli
Commissioner

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