

**Wilkinson Property Fund III LP**

**v.**

**Town of Milford**

**Docket Nos.: 15408-94PT and 16162-95PT**

**DECISION**

The "Taxpayer" appeals, pursuant to RSA 76:16-a, the "Town's" 1994 and 1995 assessments of:

\$4,461,400 (land \$1,498,600; buildings \$2,962,800) on Lot 32, a 5.91-acre lot with 4, 30-unit apartment buildings;

\$2,128,600 (land \$768,100; buildings \$1,360,500) on Lot 33, a 14-acre lot with 2, 30-unit apartment buildings; and

\$39,400 (land \$32,500; buildings \$6,900) on Lot 35, a 15,681 square-foot lot with a building.

The three lots (collectively known as the "Property") have a total assessed value of \$6,629,400 and comprise the Woodland Heights Apartments, a 180-unit apartment complex on a 21.72-acre lot. At the hearing, the Town stated that the above assessments were a result of an earlier board decision, Docket No. 14272-93PT but the Town inadvertently included the \$39,400 assessment twice and, therefore, the actual total assessments should be \$6,590,000. The complex contains 177 residential units, 1 management/office unit, 1

maintenance-shop unit, and 1 recreation-room unit. For the reasons stated below, the appeals for abatement are granted.

The Taxpayer has the burden of showing the assessments were disproportionately high or were unlawful, resulting in the Taxpayer paying a disproportionate share of taxes. See RSA 76:16-a; TAX 203.09(a); Appeal of City of Nashua, 138 N.H. 261, 265 (1994). To establish disproportionality,

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the Taxpayer must show that the Property's assessments were higher than the general level of assessment in the municipality. Id. The Taxpayer carried this burden.

At the hearing the parties stipulated to the following:

- 1) the department of revenue administration's (DRA) equalization ratio for 1994 and 1995 of 1.35 and 1.38 respectively are generally reflective of the Town's level of assessment and are to be used to equalize the board's finding of market value;
- 2) the board need only find a market value for 1994 which will be applicable to 1995 (as discussed later, the board departs from this stipulation due to the methodology the board uses in deducting the cost of deferred maintenance);
- 3) the income approach is the only approach to be considered by the board in determining the market value of the Property;
- 4) the appropriate vacancy and collection loss rate is 10%;
- 5) miscellaneous income is estimated at 3% of gross potential income;
- 6) the difference between the parties' capitalization rates of 13.9% and 14.04% is insignificant;
- 7) the Property as of 1994 had approximately \$317,000 in deferred maintenance

expenses (the parties disagreed, however, as to how the cost of deferred maintenance was to be accounted for in the Property's final determination of value); and

8) the expense analysis of 17 comparable properties contained in the Kline appraisal is appropriate for estimating the level of expenses to be deducted (however, the Taxpayer argued that the result is exclusive of reserve for replacements while the Town argued it is inclusive of reserve for replacements).

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The Taxpayer argued the assessments were excessive because:

(1) there was significant deferred maintenance on the Property requiring higher than average expenses;

(2) an April 1994 appraisal (Kline appraisal) estimated the market value to be \$3,350,000;

(3) the analysis of expenses contained in the Kline appraisal is not inclusive of replacement for reserves and an additional amount of approximately \$250 per unit should be added to the expenses;

(4) it is more appropriate to estimate expenses on a dollar amount per unit as opposed to a percentage of effective gross income because many expenses are fixed and are not in direct relationship to total rents or occupancy level; and

(5) a determination of market rent is more appropriately determined by

analyzing comparable rents rather than relying on general rent studies such as the Town's use of the New Hampshire Housing Finance Authority (NHHFA) study.

The Town argued the assessments were proper because:

- (1) using rent levels as indicated in the NHHFA study, calculating income on the total of 180 units, estimating expenses at 39% of effective gross income and not deducting a value for personal property results in an indicated market value that supports the assessment;
- (2) the Kline appraisal employed improper methodology by including the miscellaneous income prior to taking vacancy and collection loss deductions; and
- (3) reducing the assessment to that estimated by the Taxpayer would place the Property at the bottom of other apartment complexes in Town based on an assessment per unit comparison.

Subsequent to the hearing, the board took a view of the Property and four of the comparables submitted by the Taxpayer. The board found this view very helpful. First, significant testimony was presented about the effect of the immediate industrial neighborhood on the Property. The Taxpayer argued

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that the industrial properties along the road accessing the Property negatively affect rents and the Property's desirability. The Town countered by submitting a rental guide advertising the Property as being in an area of "rolling farmland and village greens". The board's view enabled us to winnow the hype from the facts. As will be discussed further in the board's specific findings, the board does find the industrial properties along the access road to the Property is a factor that affects rent levels and no slick marketing

brochure can overcome the fact. Second, the board found the view helpful in its determination of proper rents by being able to compare, at least from the exterior, the condition, quality and location of the comparable properties relative to the Property.

### **Board's Rulings**

A wise assessor once told a board member that when faced with the task of valuing a unique or difficult property, do it one step at a time. Determine the facts at each juncture, apply good judgement, perform the calculations to a bottom line and then step back and see if the end result is reasonable. That is what the board has attempted to do in this case utilizing the income approach as stipulated to by the parties and deciding on its proper components<sup>1</sup>.

The board finds the proper assessed values to be: 1994: \$5,486,200; 1995: \$5,753,700. The sole difference between the two years is the application of the different equalization ratios as stipulated to by the parties and different deductions for deferred maintenance to account for estimated improvements that occurred between the two tax years. The board will detail in its decision its various findings relative to the income approach. However, in summary, its conclusions are as follows:

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<sup>1</sup> Even if the parties had not stipulated to the income approach, the board would have placed significant weight on the income approach due to the income producing nature of the Property.

1994 Summary

Gross Potential Income	\$1,111,680
Vacancy and Collection Loss @ 10% PGI	<u>x .90</u>
	\$1,000,512
Miscellaneous Income @ 3% PGI	<u>\$ 33,350</u>
Effective Gross Income (EGI)	\$1,033,862
Expenses Including Reserve for Replacement 40%	<u>\$ 413,545</u>
Net Operating Income	\$ 620,317
Capitalization Rate @ 14%	<u>÷ .14</u>
Indicated Market Value Before Deferred Maintenance	\$4,430,850
Personal Property	<u>- 50,000</u>
Indicated Market Value Less Personal Property	\$4,380,850
Deferred Maintenance for 1994	<u>- 317,000</u>
1994 Market Value	\$4,063,850
1994 Equalization Ratio	<u>x 1.35</u>
1994 Assessed Value	\$5,486,200

1995 Summary

Indicated Market Value Before Deferred Maintenance	\$4,380,850
Deferred Maintenance for 1995	<u>- 211,500</u>
Indicated 1995 Market Value	\$4,169,350
1995 Equalization Ratio	<u>x 1.38</u>
1995 Assessed Value	\$5,753,700

**Specific Findings**

Potential Gross Income

First, the board finds the potential gross income should be calculated on the basis of 177 units as opposed to the total of 180 units. The board agrees with the Taxpayer's arguments that the three units not leased are necessary as they are used (sales office, maintenance shop and aerobics room) to support reasonable rent levels. The board finds the alternative would be for any owner of the Property to separately construct additional facilities for these purposes which would create additional capital outlay and expenses and would erode the then slightly higher gross income from 180 units. Therefore, the board concludes 177 units as the basis for the gross potential income is reasonable.

The board finds the gross potential income is calculated in detail as follows:

Apt. Type	Monthly Rent		# of Rentable Units	Month/Year	GPI per Apt. Size
Studio	\$350	x	6	x 12 months	= \$ 25,200
1 Bedroom	\$475	x	48	x 12 months	= \$ 273,600
2 Bedroom	\$550	x	122	x 12 months	= \$ 805,200
3 Bedroom	\$640	x	1	x 12 months	= <u>\$ 7,688</u>
Total Gross Potential Income					\$1,111,680

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In arriving at these monthly rents, the board considered and weighed a number of factors including: the effect of deferred maintenance on rents, the actual rents received at the Property during the years under appeal, the Kline comparable properties, especially comparable 1, Laurel Hills Apartments, the Property's rents in late 1996 and early 1997 and the Property's immediate neighborhood.

The board considered the Town's NHHFA study in the context of the other rental data but gave it little weight because it contained rents from the Manchester and Nashua market and was comprised of generally smaller complexes.

Market rent is best determined by a market analysis of properties most similar to the subject with adjustments for consideration being made for the difference. As is true in the market approach, the best comparable data is usually the most localized data that requires a minimum of adjustments.

First, in arriving at its estimates of market rent, the board kept in mind that, if a deduction for deferred maintenance was to be made at the conclusion of the income approach calculation, the rent on the front side of the calculation needed to reflect the Property with the deferred maintenance cured. While the board agrees with the Taxpayer that some of the deferred maintenance items would alone not allow for a rent increase, some items do enhance the Property's ability to improve its occupancy, client mix and rent

level. This is indeed evident by the improved rent levels reported in 1996 and 1997. The board is aware that some of the increase was due to general market improvement; however, as Ms. Kemezys, the Property's manager, testified, some of it was due to an improvement in the "tenant mix". Certainly the board has the benefit of hindsight as to the increase in the

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rents. However, a prudent investor would also assume that, with good management and correcting deferred maintenance, the quality of the "tenant mix" could be improved to allow for an increase in the rent level<sup>2</sup>.

Second, the actual rents, were given some weight by the board; however, as stated above, those rents need to be increased slightly to reflect the effects of the cured deferred maintenance.

Third, based on the evidence and the board's view, we find Laurel Hill Apartments is the most comparable complex and gave some weight to its rents. Laurel Hill Apartments, while a smaller complex, is not so small to be of a different magnitude. Based on the view it has a slightly better location with

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<sup>2</sup> In reality this slight increase of the rents and the three-year stepped down deferred maintenance deduction (discussed further on page 10) is akin to a discounted cash flow (DCF) analysis. Given the transitional nature of this Property, such approach would be reasonable in estimating market value. However, neither party performed a DCF, and the board's modification of the direct capitalization approach reflects some of the transitional aspects of the Property.

more open space and tree buffer around it. While from the exterior the condition appeared similar, Kline notes in his appraisal the condition is not as good as the Property. Laurel Hill Apartments also had a slightly better tenant mix at the time, although it also had an offsetting higher vacancy rate. The board finds any prospective purchaser could have seen Laurel Hill Apartments as an indication of the opportunity to achieve higher rents by improving the "tenant mix" over a period of years.

Fourth, as touched on earlier in this decision, the board considers the immediate neighborhood of the Property is a negative factor affecting rent levels. The approach to the Property is past eight or nine industrial/research and development buildings which, while generally neat, are quite intense and not a very compatible use with the Property's residential use (eg., the Property's swimming pool is directly adjacent to one of the industrial/R&D buildings).

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#### Proper Calculation Relative to Adding Miscellaneous Income

The board agrees with the Town that the proper procedure is to add the miscellaneous income to the rental income after vacancy and collection loss has been deducted from the gross potential income. See The International Association of Assessing Officials, Property Appraisal and Assessing Administration 255 (1990).

#### Expenses

The determination of the proper amount to be deducted for expenses was the most difficult issue for the board to reach a conclusion. However, based

on the facts in this case, we conclude it is reasonable to estimate expenses as a percentage of the effective gross income rather than as an absolute amount per unit. Further, we conclude that the expense amount per unit derived from the analysis of 17 comparables in the Kline appraisal likely includes items that for appraisal purposes would be included in a replacement for reserves account.

The Taxpayer argued that expenses as an absolute amount per unit was more appropriate than a percentage because the Property had a low rent level compared to the comparables from which the numbers were derived. While this is a reasonable argument, the board finds that there was little evidence of a unique nature for this Property, other than deferred maintenance, to justify a significantly higher level of fixed costs relative to the comparable properties. The Property is of average quality with minimal landscaping and common amenities. It is different than other properties with more expansive amenities and facilities that would be more expensive to maintain.

The board received conflicting evidence and testimony as to whether Kline had removed items normally involved in replacement for reserve accounts from the 17 properties he analyzed for expense purposes. Kline testified and presented an affidavit that he did deduct the replacement for reserve items from the expense information received from the comparables properties.

However, the board notes that nowhere in the Kline appraisal is there mention

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of this important step. The board notes that between the two days of the hearings, Kline revised a number of pages of the appraisal making corrections for the inclusion of utilities in the rental amount of some of his

comparables. Given that the issue of the inclusion of utilities in rent was a major factor in an earlier appeal of this Property, (Docket No.: 14272-93PT), the board questions whether Kline was actually as diligent in removing those items from the expense analysis as he subsequently testified to. Further, the board agrees with the Town that generally the expense information kept by these types of properties is for income tax reporting purposes. Normally, many items which for appraisal purposes are considered as replacements for reserves are included in annual expense reports for income tax purposes. In short, the board is uncertain of what was included and not included in the Kline expense analysis due to lack of supporting documentation. Therefore, the board finds the Taxpayer did not fulfill its burden of proof on this issue, and we find with the Town.

The board's choice of 40% for expenses and the resulting EGI is based on considering the Kline analysis median percentage of 39%, Kline's actual expenses excluding replacement for reserves for the Property's at 41% and the board's earlier finding of expenses for this Property in Docket No.: 14272-93PT was 40%. We do note also that the actual expenses of the Property were higher. But again, it is difficult to determine from the expense information submitted whether replacement of reserve items and deferred maintenance items were included in the Taxpayer's "routine" expenses.

#### Personal Property

The board finds that it is reasonable that a value for personal property (the kitchen and laundry, appliances not built-in) be deducted from the indicated value of the entire rentable income. Because the rents that can be obtained for the units include the presence of this personal property, they need to be removed to result in the net value attributable to the real estate.

The methodology, value and depreciation employed by Kline in his report on

pages 107 and 108 appear reasonable and consistent with how the board has adjusted for personal property in other appeals. Therefore, we find the deduction for \$50,000 of personal property is proper and reasonable.

Deferred Maintenance

The parties agreed that Kline's estimate of \$317,000 of deferred maintenance items was reasonable as to the outstanding repairs that needed to be made to the Property. However, they disagree as to how this number should be deducted from any indication of value. Again, the board would note that this issue would be more easily resolved if a DCF technique had been employed.

In a DCF, reasonable assumptions can be made as to the term over which repairs should be made and include them as expenses during those years. However, because neither party presented a DCF, the board has modified the direct capitalization approach to try to reflect the fact that the deferred maintenance is a cost that would be incurred over several years as both the Kline appraisal estimated and hindsight has shown was the case with the Property.

Because the board's rent assumes the Property has had the deferred maintenance items cured to achieve those higher rents, some deductions from the indicated market value is needed. The board finds that for 1994 the entire amount of \$317,000 is reasonable to be deducted as it is unlikely that any significant amount of the repair would have been done by April 1, 1994. The board tried to determine from the testimony and evidence as to what work actually had been done during 1994, 1995 and 1996. However, the testimony was conflicting as to the actual amount attributable to deferred maintenance

items. Consequently, the board finds that a prudent investor would project these repairs to occur over a three-year period. Thus, in 1994 the full amount of \$317,000 needs to be deducted. For 1995, the board has reduced this amount by one-third to \$211,500 on the assumption that one third of the deferred maintenance has been cured as of April 1995. This is why the board has departed from the parties stipulation that it only needed to make one

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market value finding as of 1994. We find it is reasonable because of the ongoing curing of a deferred maintenance that the values be distinct for each year. The board would note that this is similar to the general practice of municipalities annually revising assessments of buildings that have ongoing renovations occurring and valuing them for the improvements that have occurred within the past tax year.

### Conclusion

On a somewhat humorous note, the board recognizes its market value findings happen to closely coincide with the average values argued by the parties. The board assures the parties it is just that, coincidence. It has at times been inferred that the board's decisions appear to be averages of the parties' positions. This is not the case here and in most cases unless specifically stated. After hours and, in this case, days of deliberation, we do sometimes note the irony of our findings coinciding with the parties' average.

In conclusion, the board finds that its conclusion attempts to account for and combine many of the arguments made by the parties. The board recognizes that the Taxpayer may view some of the board's assumptions as aggressive. However, the Taxpayer should focus on the board's commentary that

it has attempted to do a modified DCF with its assumptions of rent and deferred maintenance calculations. Likewise, the Town should realize that some of its arguments such as the NHHFA rental survey, basing PGI on 180 units and not deducting personal property are not reasonable given the specific facts and nature of this Property.

### **Refund**

If the taxes have been paid, the amount paid on the value in excess of \$5,486,200 for 1994 and \$5,753,700 for 1995 shall be refunded with interest at six percent per annum from date paid to refund date. RSA 76:17-a. Pursuant to RSA 76:17-c II, and board rule TAX 203.05, unless the Town has undergone a general reassessment, the Town shall also refund any overpayment for 1996.

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Until the Town undergoes a general reassessment, the Town shall use the ordered assessment for subsequent years with good-faith adjustments under RSA 75:8. RSA 76:17-c I. Given the board's findings on these appeals, reasonable adjustment for continued curing of deferred maintenance in subsequent years would be good-faith adjustments.

### **Rehearing**

A motion for rehearing, reconsideration or clarification (collectively "rehearing motion") of this decision must be filed within thirty (30) days of the clerk's date below, not the date this decision is received. RSA 541:3; TAX 201.37. The rehearing motion must state with specificity all of the reasons supporting the request. RSA 541:4; TAX 201.37(b). A rehearing motion is granted only if the moving party establishes: 1) the decision needs clarification; or 2) based on the evidence and arguments submitted to the

board, the board's decision was erroneous in fact or in law. Thus, new evidence and new arguments are only allowed in very limited circumstances as stated in board rule TAX 201.37(e). Filing a rehearing motion is a prerequisite for appealing to the supreme court, and the grounds on appeal are limited to those stated in the rehearing motion. RSA 541:6. Generally, if the board denies the rehearing motion, an appeal to the supreme court must be filed within thirty (30) days of the date on the board's denial.

SO ORDERED.

BOARD OF TAX AND LAND APPEALS

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Paul B. Franklin, Chairman

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Michele E. LeBrun, Member

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**Certification**

I hereby certify a copy of the foregoing decision has been mailed this date, postage prepaid, to Peter D. Wenger, Esq., Counsel for Wilkinson Property Fund III LP, Taxpayer; William R. Drescher, Esq., counsel for the Town; and Chairman, Selectmen of Milford.

Date: May 7, 1997

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Valerie B. Lanigan, Clerk

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v.

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ORDER

This order responds to various motions filed by the parties.

- 1.The board grants the "Taxpayer's" September 18, 1996 motion for leave to use more than 10 comparables.
- 2.The board grants the "Town's" September 20, 1996 motion to continue the tentative hearing date of November 20, 1996. A firm hearing date will be decided at the prehearing conference.
- 3.The board grants the Town's September 26, 1996 motion to continue the prehearing conference. The October 23, 1996 prehearing conference is continued to **November 19, 1996 at 10:30 A.M.** in order to allow the Town adequate time to review the Taxpayer's additional comparables.
- 4.Based on the above, the prehearing conference statements and supporting documentation must be exchanged between the parties and filed with this board by November 1, 1996.

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SO ORDERED.

BOARD OF TAX AND LAND APPEALS

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Paul B. Franklin, Chairman

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Ignatius MacLellan, Esq., Member

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Michele E. LeBrun, Member

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Douglas S. Ricard, Member

CERTIFICATION

I hereby certify that copies of the foregoing order have this date been mailed, postage prepaid, to Peter D. Wenger, Esq., Counsel for Wilkinson Property Fund III LP, Taxpayer; and David M. McMullen, CNHA, Assessor for the Town of Milford.

Dated: October 17, 1996

Valerie B. Lanigan, Clerk

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