Belmar/PAG Limited Partnership

v.

City of Nashua

Docket No.: 19600-02PT

DECISION

The "Taxpayer" appeals, pursuant to RSA 76:16-a, the "City's" 2002 assessment of $2,828,200 (land $1,199,600; buildings $1,628,600) on a 45-unit elderly housing complex on 5.75 acres (the "Property"). For the reasons stated below, the appeal for abatement is granted.

The Taxpayer has the burden of showing, by a preponderance of the evidence, the assessment was disproportionately high or unlawful, resulting in the Taxpayer paying a disproportionate share of taxes. See RSA 76:16-a; TAX 201.27(f); TAX 203.09(a); Appeal of City of Nashua, 138 N.H. 261, 265 (1994). To establish disproportionality, the Taxpayer must show the Property's assessment was higher than the general level of assessment in the municipality. Id. The Taxpayer carried this burden.

The Taxpayer argued the assessment was excessive because:

(1) based on an analysis by the income approach utilizing contract rents and expenses, the Property had a market value for 2002 of between $1,910,372 and $2,177,727;

(2) the Property's income is regulated by the Section 8 subsidized housing restrictions of the department of housing and urban development ("HUD") and have increased at an annual rate of only 1% to 2%, significantly less than the increase in expenses;

(3) the Property is approaching 25 years in age and is facing several significant maintenance/replacement issues such as new roofs, replacement of existing windows with more energy efficient ones, replacement and improvement of appliances to make some units handicap accessible, replacement of carpets, etc.;

(4) a change in regulations relative to parking spaces for handicap accessible vehicles has necessitated, subsequent to 2002, the construction of additional parking spaces;

(5) capitalization rates for noninstitutional properties have not decreased significantly since the board's decision in this case for tax year 1999 (Docket No.: 18345-99PT), the equity rate component of a capitalization rate for the Property has also not decreased as any prospective purchaser would be concerned with the impending maintenance and replacement issues with the Property; and

(6) the stoves and refrigerators in each of the 45 units and the common area are personal property (the two totaling an estimated $37,500) and should be deducted from any final market value estimate for the Property.

The City recommended a revised assessment of $2,312,600 based on a market value estimate of $3,100,000 and the department of revenue administration's ("DRA") 2002 equalization ratio of .746. The City argued the recommended assessment was proper because:

(1) since the board's prior decision for tax year 1999, interest rates have dropped significantly, and thus, the overall capitalization rate found by the board in 1999 is no longer applicable; and

(2) the City's summary appraisal estimated a market value as of April 1, 2002 of $3,100,000 based on stabilizing the prior three years actual income and expense information and estimating an overall capitalization rate (inclusive of effective tax rate) of 8.24%.

The parties stipulated the level of assessment was reasonably estimated at .746 based on the DRA's 2002 equalization ratio. The parties also stipulated the City performed no reassessment or any good faith change for tax year 2003 but did for 2004. Consequently, any abatement ordered by the board would apply for tax years 2002 and 2003 only.

BOARD'S RULINGS

General Findings

Based on the evidence, the board finds the proper assessment to be $1,893,400, based on a market value estimate of $2,538,057 and the 2002 level of assessment of .746.

This Property was appealed to the board for tax year 1999 (Docket No.: 18345-99PT) and, as the parties agreed, the "general" findings made in the 1999 earlier decision apply to this 2002 appeal. In short, the Property has 45 units of subsidized housing regulated by agreements with HUD which both positively and negatively affect the Property's value. Further, governmental regulations must be considered in valuing such a property, and thus, the income approach utilizing the contract regulated rents and reasonable expenses form the most appropriate basis in estimating the Property's value.

In estimating reasonable potential gross income, vacancy rate, expenses and overall capitalization rate, the board has reviewed the financial statements submitted by both parties in a manner that a prospective purchaser would likely do to estimate what projected income and expenses would be for tax year 2002.

In doing so, the board concludes the City's averaging of the board's 1999 findings with the 2000 and 2001 income and expense estimates to arrive at stabilized income and expense information is not what a prospective purchaser would do. While a purchaser would certainly look at historical information, they would not assume the projected 2002 income and expenses are an average of the previous three years. Rather, they would look at the trends of income and expenses exhibited in the prior years and attempt to project those trends in a knowledgeable manner to arrive at estimated 2002 income and expense figures.

Similarly, when determining what a reasonable capitalization rate would be, the board finds that a prospective purchaser would not necessarily be influenced by national capitalization rates, as presented by the Taxpayer, as much as they would by more localized market mortgage and equity rates. The board also finds a prospective knowledgeable purchaser would be aware of the limited increase in the income stream but also consider the guarantees of such income stream based on the federal subsidy and the high demand for affordable housing in this area of the state.

SPECIFIC FINDINGS

The board's findings relative to income, expense and capitalization rates are summarized below. Detailed findings following the summary relative to the various components of the income approach.

Potential Gross Income	$490,860
Vacancy - .75%	$ 3,681
Effective Gross Income	$487,179
Expenses	
Administrative	$ 83,500
Utilities	$ 68,000
Operating and Maintenance	$ 75,000
Insurance and Payroll Taxes	$ 22,000
Replacement Reserves	$ 10,000
Total Expenses	$258,500
Net Operating Income(NOI)	$228,679
Capitalization Rate	.0725
Effective Tax Rate	.0176
Overall Capitalization Rate	.0901
Indicated Market Value (NOI $228,679 ÷ .0901)	$2,538,057
2002 Equalization Ratio	x .746
2002 Assessed Value	$1,893,400 (rounded)

Potential Gross Income

The Taxpayer estimated potential gross income ("PGI") of $485,271 for 2000 and $487,388 for 2001. The City had stabilized the PGI at $485,878. The Taxpayer's 2000 and 2001 PGIs are true PGI figures as they are estimates pulled from the financial statement indicating the total potential rent that could be obtained from the 45 units if no vacancy occurred. The City's stabilized income is based on actual rental income received rather than potential rent, and thus, reflects the historical vacancies. The City, however, also added over $6,000 for interest, air conditioning and vending charges. Regardless, both parties are reasonably close in their estimates of a PGI based on historical information of approximately $486,000. To estimate what the PGI might be for 2002, the board has considered the evidence of the historical annual income increases of approximately 1% and applied it to an estimate (including some income for laundromat income) of $486,000 ($486,000 x 1.01 = $490,860).

Vacancy

The board finds the City's estimate of .75% vacancy is supported generally by the historical vacancy figure estimates and by the testimony that, in most cases, the units, when vacant, are retrofitted and available for occupancy in a matter of a couple of weeks. Further, the board considered the clarification presented at hearing of the evidence in the 1999 appeal that HUD does subsidize vacancy but only at 80% of the permitted rent and only for the time the unit is available for occupancy, but not occupied. All the evidence indicates there is a strong demand for such units, and thus, the risk of any unit remaining vacant is negligible as reflected in the historical vacancy rate.

Expenses Generally

In estimating projected expenses for 2002, the board reviewed both the three-year (2000–2002) statements of profit and loss ("P&L Statements") filings with HUD and the audited statements of cash flow that are contained in Taxpayer Exhibit 1. While the P&L Statements and the audited statements of cash flow generally agree, there are some discrepancies the board was unable to reconcile. Consequently, in projecting estimated expenses, the board has relied primarily on the P&L Statements as they provide a greater level of detail and breakdown of the categorized expenses.

Administrative Expenses

The board has estimated the administrative expenses at $83,500 by reviewing the detailed entries of the 2000 and 2001 P&L Statements and applying a similar rate of increase to the 2001 actuals (approximately 3.5%) as indicated by the increase from 2000 to 2001.

Utilities

The board has estimated $68,000 for utilities based on a review of the prior three years' utilities expenses. No evidence was submitted as to why the utility expenses have fluctuated in an inconsistent fashion over the past several years. However, the board believes that any prospective purchaser would budget certainly for no less than what the utility expenses have been in recent years, and thus, we have estimated $68,000.

Operating and Maintenance Expenses

The board has estimated $75,000 for operating and maintenance expenses based on a review of the 2000-2001 actuals. While on a percentage basis, the operating and maintenance expenses increased by approximately 8%, most of that is due to an unexplained increase in the heating and cooling repairs and maintenance in 2001 going from approximately $1,200 in 2000 to almost $12,000 in 2001. Given that the Property is heated with electricity and has window air conditioning units, no logic or evidence explains this dramatic increase, and thus, the board has stabilized this expense estimate at $75,000.

Insurance and Payroll Taxes

Both parties in their income analysis included as an insurance expense the costs related to property and liability insurance for the Property. However, in reviewing the details of the P&L Statements, the board notes they contain a number of other employee related expenses such as workman's compensation, health insurance and payroll taxes that should also be included as an expense deduction as they relate to the operating expenses of the Property. Despite the testimony of the Taxpayer that insurance costs had risen dramatically, the P&L Statements do not indicate that, even when the subsequent information contained in the 2002 P&L Statement is

considered. The payroll taxes, employee related insurance and property related insurance for 2000 and 2001 range from $16,303 to $20,421. The board, based on these two years' historical information, has projected an expense of $22,000 for 2002.

Replacement Reserves

Mr. Greg Jenner, senior property manager for the Property, testified to a number of short term capital items that have been or remain to be addressed with the Property, including converting some units for handicapped accessibility, replacement of bathroom and kitchen fixtures and appliances, windows, carpets and ultimately, at some point, the roofs. The board finds, based on the evidence, that any prospective purchaser would be aware of the age of the Property and that a number of these capital replacement items would need to be addressed during the holding period of the Property. Thus, any valuation by the income approach must attempt to estimate the cost of these items by adequate replacement reserves. The actuals, that were both testified to and indicated in the financial statements, vary from year to year based on the projects undertaken in that year, and thus, do not form the sole basis for estimating a pro forma amount to be included in an income approach analysis. The board acknowledges that actual expenditure of such funds will vary from year to year and, while no specific evidence was submitted on this issue, frequently some replacement reserve items get "expensed" in the annual operating expenses. Nonetheless, on balance, the board believes the $10,000 recommended in Taxpayer Exhibit 1 income analysis is a reasonable annual estimate for replacement reserves.

Capitalization Rate

The board estimates a capitalization rate, exclusive of the effective tax rate, at 7.25%. The board finds the general market evidence of regional (Northern New England and New Hampshire) capitalization rates as discussed, in particular, by the City, the best evidence

submitted. The board finds the Taxpayer's assertion of a higher capitalization rate based on national reporting entities is not conclusive of what a prospective purchaser would be able to acquire the Property for based on localized market rates and equity return expectations. The board agrees with the City that housing demands and needs in southern New Hampshire, particularly for low income housing, are extremely high. Also, estimating market value by the income approach and relying on historical income and expense data to project income expenses for 2002 and including an increased replacement reserve expense diminishes significantly the remaining risk or uncertainty to any owner of the Property. As a result, we find an equity rate estimate would be closer to the City's than the 20% argued by the Taxpayer. On the other hand, the board finds it is difficult to accept the City's capitalization rate of 6.48% as it is lower than capitalization rates derived directly from the market that the City testified to as being in the 7% to 7.5% range for larger, more institutional grade investment properties. Balancing the various evidence submitted, the board has estimated the capitalization rate at 7.25% and added to it the effective tax rate of 1.76%.

Personal Property

As in its 1999 decision, the board addressed the washer and dryer personal property income stream by reducing the vending income slightly. The Taxpayer presented additional arguments in its 2002 appeal (that it did not present in its 1999 appeal) relative to a further personal property deduction for the stoves and refrigerators in the units and the common area personal property. While conceivably such items do contribute slightly to the income stream, the board is not deducting any estimate of personal property for several reasons. First, the Taxpayer's estimate of $37,500 lacks any detail as to how the estimate was arrived at. For example, no information was submitted as to the age and original cost of the various personal

property items whose value is being estimated. Second, the board reviewed the photographs submitted of the items and based simply on that evidence, believes that such personal property items are generally of low value and, in the overall scheme of the value of the Property, have a very nominal contribution to the income stream. Third, no evidence was submitted but the board finds it is possible the periodic replacement of such items could actually be part of the maintenance and operation expenses as opposed to being replacement of capital items under replacement reserves. For the Taxpayer to prevail on this issue, more evidence needs to be submitted as to the nature of the items, their value and the manner in which they are maintained relative to the income and expense information utilized in establishing the Property's market value by the income approach.

If the taxes have been paid, the amount paid on the value in excess of $1,893,400 shall be refunded with interest at six percent per annum from date paid to refund date. RSA 76:17-a. As the City had performed a reassessment for tax year 2004, as stipulated by the parties, the City shall also use the ordered assessment for tax year 2003. RSA 76:17-c, I and II.

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, <u>not the date this decision is received</u>. 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(f). 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

Certification

I hereby certify a copy of the foregoing Decision has this date been mailed, postage prepaid, to: Mark Lutter, Northeast Property Tax Consultants, Post Office Box 735, Derry, New Hampshire 03038, representative for the Taxpayer; and Chairman, Board of Assessors, Post Office Box 2019, Nashua, New Hampshire 03061.

Date: July 20, 2005

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Anne M. Stelmach, Clerk