

**BEFORE THE NEBRASKA TAX EQUALIZATION AND REVIEW COMMISSION**

Woodside Place, Inc.,  
Appellant,

v.

Lancaster County Board of Equalization,  
Appellee.

Case No: 12R 804

Decision and Order Affirming the  
Determination of the Lancaster County  
Board of Equalization

**For the Appellant:**

Dan Kubr,  
President of Woodside Place, Inc.

**For the Appellee:**

Richard Grabow,  
Deputy Lancaster County Attorney.

This appeal was heard before Commissioners Robert W. Hotz and Nancy J. Salmon.

**I. THE SUBJECT PROPERTY**

The Subject Property is a residential parcel located at 2900 Merrill Street, Lincoln, Lancaster County, Nebraska. The parcel is improved with five duplexes, consisting of four three-bedroom units and six two-bedroom units, all subject to rent restrictions under a land use restriction agreement (LURA),<sup>1</sup> and all participating in a Section 42, low-income housing tax credit (LIHTC) program.<sup>2</sup> The legal description of the parcel and the Property Record Card for the Subject Property is found at Exhibit 2, pages 6-12.

**II. PROCEDURAL HISTORY**

The Lancaster County Assessor (the County Assessor) determined that the assessed value of the Subject Property was \$594,900 for tax year 2012.<sup>3</sup> Woodside Place, Inc. (the Taxpayer) protested this assessment to the Lancaster County Board of Equalization (the County Board) and

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<sup>1</sup> Exhibit 3:148-183.

<sup>2</sup> See generally 26 U.S.C. §42.

<sup>3</sup> See, E1:1.

requested an assessed valuation of \$386,700.<sup>4</sup> The County Board determined that the taxable value of the Subject Property for tax year 2012 was \$594,900.<sup>5</sup>

The Taxpayer appealed the decision of the County Board to the Tax Equalization and Review Commission (Commission). Prior to the hearing, the parties exchanged exhibits and submitted a Pre-Hearing Conference Report, as ordered by the Commission. The Commission held a hearing on October 30, 2014.

### III. STANDARD OF REVIEW

The Commission's review of the determination by a County Board of Equalization is de novo.<sup>6</sup> When the Commission considers an appeal of a decision of a County Board of Equalization, a presumption exists that the "board of equalization has faithfully performed its official duties in making an assessment and has acted upon sufficient competent evidence to justify its action."<sup>7</sup>

That presumption remains until there is competent evidence to the contrary presented, and the presumption disappears when there is competent evidence adduced on appeal to the contrary. From that point forward, the reasonableness of the valuation fixed by the board of equalization becomes one of fact based upon all the evidence presented. The burden of showing such valuation to be unreasonable rests upon the taxpayer on appeal from the action of the board.<sup>8</sup>

The order, decision, determination or action appealed from shall be affirmed unless evidence is adduced establishing that the order, decision, determination, or action was unreasonable or arbitrary.<sup>9</sup> Proof that the order, decision, determination, or action was unreasonable or arbitrary must be made by clear and convincing evidence.<sup>10</sup>

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<sup>4</sup> See, E2:5.

<sup>5</sup> See, E1:1.

<sup>6</sup> See, Neb. Rev. Stat. §77-5016(8) (2012 Cum. Supp.), *Brenner v. Banner Cty. Bd. Of Equal.*, 276 Neb. 275, 286, 753 N.W.2d 802, 813 (2008). "When an appeal is conducted as a 'trial de novo,' as opposed to a 'trial de novo on the record,' it means literally a new hearing and not merely new findings of fact based upon a previous record. A trial de novo is conducted as though the earlier trial had not been held in the first place, and evidence is taken anew as such evidence is available at the time of the trial on appeal." *Koch v. Cedar Cty. Freeholder Bd.*, 276 Neb. 1009, 1019 (2009).

<sup>7</sup> *Brenner v. Banner Cty. Bd. Of Equal.*, 276 Neb. 275, 283, 753 N.W.2d 802, 811 (2008) (Citations omitted).

<sup>8</sup> *Id.*

<sup>9</sup> Neb. Rev. Stat. §77-5016(8) (2012 Cum. Supp.).

<sup>10</sup> *Omaha Country Club v. Douglas Cty. Bd. of Equal.*, 11 Neb. App. 171, 645 N.W.2d 821 (2002).

A Taxpayer must introduce competent evidence of actual value of the subject property in order to successfully claim that the subject property is overvalued.<sup>11</sup> The County Board need not put on any evidence to support its valuation of the property at issue unless the taxpayer establishes the Board's valuation was unreasonable or arbitrary.<sup>12</sup>

In an appeal, the commission “may determine any question raised in the proceeding upon which an order, decision, determination, or action appealed from is based. The commission may consider all questions necessary to determine taxable value of property as it hears an appeal or cross appeal.”<sup>13</sup> The commission may also “take notice of judicially cognizable facts and in addition may take notice of general, technical, or scientific facts within its specialized knowledge...,” and may “utilize its experience, technical competence, and specialized knowledge in the evaluation of the evidence presented to it.”<sup>14</sup> The Commission’s Decision and Order shall include findings of fact and conclusions of law.<sup>15</sup>

#### IV. VALUATION

##### A. Applicable Law

The Nebraska Investment Finance Authority (NIFA) is a quasi-governmental body<sup>16</sup> and a body politic and corporate. NIFA is not a state agency.<sup>17</sup> The Commission’s Rules and Regulations provide that the Commission may consider and utilize “the laws of the United States and any amendments thereto.” This would include Title 26 of the United States Code, including section 42 of the same concerning the low-income housing tax credit program and all other referenced statutes in the same title, and “the Code of Federal Regulations and any amendments thereto[.]”<sup>18</sup>

Title 26 of the United States Code, including section 42, contains the federal legislation applicable to the low-income housing tax credit program, and establishes definitions for the

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<sup>11</sup> Cf. *Josten-Wilbert Vault Co. v. Board of Equalization for Buffalo County*, 179 Neb. 415, 138 N.W.2d 641 (1965) (determination of actual value); *Lincoln Tel. and Tel. Co. v. County Bd. Of Equalization of York County*, 209 Neb. 465, 308 N.W.2d 515 (1981)(determination of equalized taxable value).

<sup>12</sup> *Bottorf v. Clay County Bd. of Equalization*, 7 Neb.App. 162, 580 N.W.2d 561 (1998).

<sup>13</sup> Neb. Rev. Stat. §77-5016(8) (2012 Cum. Supp.).

<sup>14</sup> Neb. Rev. Stat. §77-5016(6) (2012 Cum. Supp.).

<sup>15</sup> Neb. Rev. Stat. §77-5018(1) (2012 Cum. Supp.).

<sup>16</sup> Neb. Rev. Stat. §58-203(1) (Reissue 2009).

<sup>17</sup> Neb. Rev. Stat. §58-226(1) (Reissue 2009).

<sup>18</sup> Neb. Rev. Stat. §77-5016(3), 442 Neb. Admin. Code, ch. 5 §031.01 (06/11).

same.<sup>19</sup> The following terms are applicable to the adjudication of this appeal and are defined by federal law: (1) low-income unit; (2) applicable percentage; (3) qualified basis; (4) applicable fraction; (5) floor space fraction; (6) eligible basis; (7) adjusted basis; and (8) basis.

The basis of property is defined as “the cost of such property[.]”<sup>20</sup> The adjusted basis is “[t]he cost of property acquired, increased for any capital improvements and decreased by the amount of depreciation allowed or allowable.”<sup>21</sup> Depreciation is not applicable to determining the qualified basis for LIHTC calculations.<sup>22</sup> The adjusted basis is determined generally through the provisions of 26 U.S.C. §1016. Portions of the basis of LIHTC properties, called the adjusted basis, are used to calculate the yearly tax credits.<sup>23</sup>

The qualified basis is determined by calculating the applicable fraction of the eligible basis.<sup>24</sup> The applicable fraction represents the lesser of the unit fraction or the floor space fraction.<sup>25</sup> The unit fraction is represented by the equation: number of low-income units divided by number of residential rental units. The floor space fraction is represented by the equation: Total floor space of low-income units divided by total floor space of residential rental units

The eligible basis for new buildings is the adjusted basis of the property at “the close of the 1<sup>st</sup> taxable year of the credit period.”<sup>26</sup> In other words, for a new building the eligible basis should equal the adjusted basis. The eligible basis used in the calculation of tax credits from year to year is fixed as of the first taxable year of the credit period, and does not change at any time during the credit period.

The yearly tax credit is calculated by finding 70% of the qualified basis for each new low-income building.<sup>27</sup> The credits are then equally distributed over 10 years. A low-income building is defined as any building that is part of a low-income project.<sup>28</sup> A low-income unit is a unit which is both rent-restricted to 30% of a tenant’s imputed income limitations and occupied by a qualified tenant under the LURA.

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<sup>19</sup> See, 26 U.S.C. §42.

<sup>20</sup> 26 U.S.C. §1012(a)

<sup>21</sup> Definition for “adjusted basis,” Black’s 6<sup>th</sup> Edition, pg. 152 (citing 26 U.S.C. §1011).

<sup>22</sup> See, 26 U.S.C. §42 (c)(4)(d).

<sup>23</sup> See, 26 U.S.C. §42 (a)(2).

<sup>24</sup> 26 U.S.C. §42 (c)(1)(A).

<sup>25</sup> 26 U.S.C. §42 (c)(1)(B).

<sup>26</sup> 26 U.S.C. §42 (d)(1).

<sup>27</sup> See, 26 U.S.C. §42 (a) – (b).

<sup>28</sup> See, 26 U.S.C. §42 (2)(A).

Under Nebraska law,

[a]ctual value is the most probable price expressed in terms of money that a property will bring if exposed for sale in the open market, or in an arm's length transaction, between a willing buyer and a willing seller, both of whom are knowledgeable concerning all the uses to which the real property is adapted and for which the real property is capable of being used. In analyzing the uses and restrictions applicable to real property the analysis shall include a full description of the physical characteristics of the real property and an identification of the property rights valued.<sup>29</sup>

“Actual value may be determined using professionally accepted mass appraisal methods, including, but not limited to, the (1) sales comparison approach using the guidelines in section 77-1371, (2) income approach, and (3) cost approach.”<sup>30</sup> “Actual value, market value, and fair market value mean exactly the same thing.”<sup>31</sup> Taxable value is the percentage of actual value subject to taxation as directed by section 77-201 of Nebraska Statutes and has the same meaning as assessed value.<sup>32</sup> All real property in Nebraska subject to taxation shall be assessed as of January 1.<sup>33</sup> All taxable real property, with the exception of agricultural land and horticultural land, shall be valued at actual value for purposes of taxation.<sup>34</sup>

Nebraska Statutes require county assessors to perform an income approach calculation for all rent-restricted housing projects<sup>35</sup> and prohibit county assessors from including as income in this calculation any tax credits received.<sup>36</sup> Such tax credits may be considered when determining the capitalization rate when capitalizing the income stream.<sup>37</sup> Rules and regulations adopted by the Nebraska Department of Revenue further establish procedures for determining the actual value of rent-restricted properties for ad valorem tax purposes.<sup>38</sup> Specifically, rent for rent-restricted units should not include the allowance for utilities.<sup>39</sup> Contract rent, economic rent or market

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<sup>29</sup> Neb. Rev. Stat. §77-112 (Reissue 2009).

<sup>30</sup> *Id.*

<sup>31</sup> *Omaha Country Club v. Douglas County Board of Equalization, et al.*, 11 Neb.App. 171, 180, 645 N.W.2d 821, 829 (2002).

<sup>32</sup> Neb. Rev. Stat. §77-131 (Reissue 2009).

<sup>33</sup> See, Neb. Rev. Stat. §77-1301(1) (Reissue 2009).

<sup>34</sup> Neb. Rev. Stat. §77-201(1) (Reissue 2009).

<sup>35</sup> See, Neb. Rev. Stat. §77-1333 (Reissue 2009). The requirement applies to projects where rent restrictions are allowed under Section 42 of the Internal Revenue Code and which have been approved by the Nebraska Investment Finance Authority (NIFA).

<sup>36</sup> See, Neb. Rev. Stat. §77-1333 (Reissue 2009).

<sup>37</sup> See, Neb. Rev. Stat. §77-1333 (Reissue 2009).

<sup>38</sup> See, 350 Neb. Admin. Code, Ch. 51 (3/09).

<sup>39</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01A(6) (3/09).

rent, Fair Market Rent (FMR), and Maximum Restricted Rent, are terms of art in the assessment of rent-restricted property in Nebraska.<sup>40</sup>

Contract rent, also known as actual rent, is the rent actually received for the units at any given time.<sup>41</sup> Economic rent or market rent is the amount of rent a property would receive on the open market without rent restrictions.<sup>42</sup> FMR is a term that describes “the maximum rent allowed to be collected on housing units subject to federal subsidy payments.”<sup>43</sup> FMR is developed by the Department of Housing and Urban Development (HUD) for the Lincoln area, Omaha area, South Sioux City area, and then for any individual county in Nebraska not included in the preceding three areas.<sup>44</sup> FMR is published annually.<sup>45</sup> “Maximum restricted rent is the maximum rent allowed to be collected on housing units subject to the applicable restrictions.”<sup>46</sup> Maximum restricted rent may be different for each rent-restricted property, and depends upon the unique target levels contained in the LURA for each property and the median incomes published by HUD.<sup>47</sup>

Rules and Regulations promulgated by the Nebraska Department of Revenue contain instructions for use of the cost approach, sales comparison approach, and income approach when valuing rent-restricted properties.<sup>48</sup> When an assessor or appraiser uses the income approach to value a rent-restricted property, the potential gross income (PGI) should be calculated “using the lesser of market rent or the Maximum Restricted Rent[.]”<sup>49</sup> When determining the capitalization rate, the assessor or appraiser must consider the tax credits, rental rates, and restrictions using generally accepted appraisal methods.<sup>50</sup>

## **B. Summary of the Evidence**

Dan Kubr, President of Woodside Place, Inc., testified that the Subject Property consists of ten rent-restricted units as part of the low-income housing tax credit program commonly referred

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<sup>40</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 E, F, G, and H (3/09).

<sup>41</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 E; See also, 350 Neb. Admin. Code, Ch. 51 §004.06C (3/09).

<sup>42</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 F; See also, 350 Neb. Admin. Code, Ch. 51 §004.06A (3/09).

<sup>43</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 G (3/09).

<sup>44</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 G (3/09).

<sup>45</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 G (3/09).

<sup>46</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 H (3/09); See also, 350 Neb. Admin. Code, Ch. 51 §004.06B (3/09).

<sup>47</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 H (3/09); See also, 350 Neb. Admin. Code, Ch. 51 §004.06B (3/09).

<sup>48</sup> See, 350 Neb. Admin. Code, Ch. 51 §005 (3/09).

<sup>49</sup> 350 Neb. Admin. Code, Ch. 51 §005.04A (3/09).

<sup>50</sup> 350 Neb. Admin. Code, Ch. 51 §005.04E (3/09).

to as Section 42, and that the owners had received \$350,430 in low-income housing tax credits over the applicable ten-year tax credit period. Kubr provided the historical expenses of the Subject Property and asserted that the rent restrictions prevent the ability to adequately pass through the expenses to the tenants.<sup>51</sup> He asserted that because the expenses could not be adequately passed through to the tenants, it would be difficult to sell the Subject Property.

Kubr did not agree with an appraisal that was completed by Great Plains Appraisal, Inc.,<sup>52</sup> but he did not have a specific opinion of the market value of the Subject Property. He also testified that the Taxpayer has never attempted to sell the Subject Property or placed the Subject Property for sale on the market. He asserted that a potential buyer's biggest consideration would be the income that could be derived from the Subject Property. Kubr asserted that owners can sell Section 42 rent-restricted properties before the end of the extended use period, but they are unable to take advantage of the equity they built up in the property because the equity must be passed on to the new owner.

Faith Medina, a full-time employee of Crown Point Management, the Property Manager of the Subject Property, testified on behalf of the Taxpayer. Medina testified regarding the current rent structure of the Subject Property, and the listed rental rates of some alleged comparable rent-restricted properties.<sup>53</sup> She asserted that these rental rates are available for viewing by the public online, and that the rental rates indicate that the Subject Property is charging rental rates similar to the rental rates charged by other rent-restricted properties in Lincoln, Nebraska. Medina also testified about the maximum rental rates, income limits, and utility allowances affecting the Subject Property for tax year 2014.<sup>54</sup> Medina testified that although she could not point to a specific section of law or the LURA, she believed all of the units of the Subject Property were restricted from being leased to anyone who exceeded 60% of the federally derived median income.

Thomas Kubert, a Certified General Appraiser in Nebraska and President of Great Plains Appraisal, Inc., testified he completed an appraisal of the Subject Property retrospective to

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<sup>51</sup> See, E22.

<sup>52</sup> The Appraisal was completed by Thomas W. Kubert and Lori L. Johnson, both holding Nebraska certificates as Certified General Real Property Appraisers, for the County Board. See Exhibit 3.

<sup>53</sup> Exhibit 22:2.

<sup>54</sup> Exhibit 22:3-4.

January 1, 2012.<sup>55</sup> He described rent-restricted properties as difficult to value because the LURA restricts the rights of use, and he was not aware of any arm's length transactions involving Section 42 properties in Nebraska.

Kubert's appraisal report contains a cost approach, a sales comparison approach, and an income approach to value the Subject Property as if unencumbered by the LURA.<sup>56</sup> Kubert's unencumbered cost approach produced an opinion of value of \$643,000,<sup>57</sup> and his reconciled sales comparison approach produced an opinion of value of \$600,000.<sup>58</sup> Kubert also conducted a direct capitalization income approach for the Subject Property as though unencumbered. He used ten alleged comparable properties,<sup>59</sup> derived market variables,<sup>60</sup> and determined an actual value of \$598,000.<sup>61</sup>

Kubert also conducted an income approach of the Subject Property as encumbered under the LURA.<sup>62</sup> He assumed that all units were rent-restricted. He asserted that the expenses for rent-restricted properties are higher and supported that assertion with expense ratios from alleged comparable properties.<sup>63</sup> He asserted that he could not load the capitalization rate with the effective tax rate so he included taxes in the expenses.<sup>64</sup>

Kubert conducted a discounted cash flow analysis (DCF), and asserted that it would be the best practice to consider the tax credits over the full 33 years of the Subject Property's restriction period even though all of the tax credits were accumulated and distributed by the end of the first ten years, because the income from the sale of the tax credits could be retained and used to offset expenses throughout the life of the Subject Property.<sup>65</sup> Kubert testified that his reading of the Subject Property's LURA indicated that the Taxpayer only received \$35,043 of tax credits over ten years, but if the actual tax credits received were approximately \$350,000, then the value of

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<sup>55</sup> See, E3.

<sup>56</sup> See, E3:83-86.

<sup>57</sup> See, E3:86.

<sup>58</sup> See, E3:100.

<sup>59</sup> See, E3:103-112.

<sup>60</sup> See, E3:114-119.

<sup>61</sup> See, E3:120.

<sup>62</sup> See, E3:101-128.

<sup>63</sup> See, E3:127.

<sup>64</sup> See, E3:127.

<sup>65</sup> See, E3:129-133.



the Subject Property as encumbered by the LURA would be significantly higher than the opinion of value derived from his DCF.

Kubert derived a capitalization rate of 4.16% based on the net operating income to discounted cash flow analysis,<sup>66</sup> and supported this capitalization rate by a band of investment analysis based on factors applicable to rent-restricted properties.<sup>67</sup> Kubert asserted that his appraisal deviated from the Department of Revenue's Rules and Regulations by not loading the capitalization rate in the DCF. Kubert asserted that he used the three year history of the Subject Property to derive the net operating income because he assumed the owners were maximizing their tenant mix, but he also asserted that he knew the net operating income as derived from the operating history was not based on the maximum restricted rent, meaning the maximum amount of rent that the owners could charge if they occupied the units with higher-income tenants that still qualified for Section 42 housing. He also asserted that the Department of Revenue's Rules and Regulations require a direct capitalization approach, but he decided to instead use a discounted cash flow analysis because there was not a stabilized income stream over the life of the Subject Property. Specifically, the tax credits are only distributed over the first ten years of the low-income project. Kubert determined that the tax credits were income, and should be included in the income instead of in the capitalization rate as required by the Department of Revenue's Rules and Regulations.

Kubert asserted his retrospective opinion of the market value of the Subject Property was \$600,000. Kubert testified that his retrospective opinion of the value of the Subject Property as restricted by the LURA was \$500,000. He also maintained that had he known that the tax credits were \$350,430, rather than \$35,043, his opinion regarding the encumbered value of the Subject Property would have been significantly higher. However, Kubert asserted that any value that took into account the LURA and tax credits amounted to an investment value, and that in his opinion the market value as unencumbered by the LURA was a better indicator of actual value of the Subject Property.

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<sup>66</sup> See, E3:131.

<sup>67</sup> See, E3:131.

### **C. Analysis of the Evidence**

The current case presents significant issues including: (1) what portion of the Subject Property is rent-restricted by law as opposed to managerial decisions; (2) whether the Subject Property operates within a sub-market of low-income projects that only attracts lower low-income tenants; (3) what is the applicability, if any, of an opinion of value for low-income projects as if not subject to the benefits and restrictions associated with the Section 42 program; and (4) what is the correct method of applying the income approach under Nebraska law when valuing rent-restricted properties for purposes of ad valorem taxes in Nebraska?

The actual value of the Subject Property must be based on the applicable restrictions on the Subject Property and the benefits afforded the Subject Property as part of the Section 42 program and the impact of the benefits and restrictions on the desirability of the Subject Property on the open market.<sup>68</sup>

The Taxpayer asserts that the County Board's determination does not accurately reflect the impact of the Subject Property's benefits and restrictions on the amount that a knowledgeable buyer would be willing to pay for the Subject Property on the open market. The Taxpayer presented some evidence regarding the Subject Property's benefits and restrictions, but did not present a separate opinion of value. For the reasons that follow, the Commission finds that the Taxpayer's evidence does not constitute clear and convincing evidence that the County Board was unreasonable or arbitrary.

Kubert presented evidence concerning the actual value of the Subject Property. Kubert arrived at an opinion of value he described as encumbered where he took into account the Subject Property's benefits and restrictions, and an unencumbered opinion of value which valued the Subject Property as though it was not affected by the Section 42 benefits and restrictions. Kubert's unencumbered opinion of value is similar to the County Board's determination, and his encumbered value is significantly less. For the following reasons, the Commission also finds that neither Kubert's appraisal, nor the totality of the evidence, constitutes clear and convincing evidence that the County Board's determination was unreasonable or arbitrary.

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<sup>68</sup> See, 350 Neb. Admin. Code, Ch. 51 §001.02 (3/09).

## 1. NIFA Requirements

Both parties made reference to NIFA requirements when discussing the restrictions placed upon the Subject Property, but neither party provided copies of the referenced requirements. NIFA is a quasi-governmental body,<sup>69</sup> a body politic and corporate, and not a state agency.<sup>70</sup> The Commission's Rules and Regulations do not permit the Commission to consider and utilize the NIFA requirements without making the document part of the record.<sup>71</sup> However, the Commission's Rules and Regulations do provide for consideration and utilization of "the laws of the United States and any amendments thereto[.]" including Title 26 of the United State Code, Section 42.<sup>72</sup> Therefore, the Commission will examine any LIHTC requirements for the Subject Property based upon the LURA, Nebraska Law, and the United States Code.

## 2. 100% of the Subject Property is Rent-Restricted

The addendum to the LURA requires that the Taxpayer maintain the applicable fraction and eligible basis so that the qualified basis for the Subject Property does not decrease.<sup>73</sup> Federal legislation, effective for tax year 1993, required an extended low-income housing commitment for all LIHTC properties in order for the owners to obtain tax credits for tax year 1993.<sup>74</sup> An extended low-income housing commitment is an agreement between the owner of the LIHTC property and the state financing authority that "the applicable fraction ... for each tax year in the extended use period will not be less than the applicable fraction specified in such agreement[.]"<sup>75</sup>

In this case, the Taxpayer had to enter into an addendum to the LURA with NIFA for an extended use period, which was specified as 15 years in the LURA.<sup>76</sup> NIFA and the Taxpayer agreed that the applicable fraction that could not decrease was the same applicable fraction determined at the end of the first taxable year of the credit period.<sup>77</sup> Therefore, starting in tax year 1993, the Taxpayer had to allocate for low-income housing the lesser of the same number of units or same amount of floor space that was allocated as of the end of the first taxable year of

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<sup>69</sup> Neb. Rev. Stat. §58-203(1) (Reissue 2009).

<sup>70</sup> Neb. Rev. Stat. §58-226(1) (Reissue 2009).

<sup>71</sup> See, Neb. Rev. Stat. §77-5016(3)(2012 Cum. Supp.), 442 Neb. Admin. Code, ch. 5 §031 (06/11).

<sup>72</sup> See, 442 Neb. Admin. Code, ch. 5 §031 (06/11).

<sup>73</sup> See, E3:177 (addendum to LURA, section 6 (3)).

<sup>74</sup> See, 26 U.S.C. §42 (h)(6).

<sup>75</sup> See, 26 U.S.C. §42(h)(6)(i).

<sup>76</sup> E3:160.

<sup>77</sup> E3:160.

the credit period for the remainder of the 15 year credit period and for the 15 year extended use period thereafter. Additionally, the Taxpayer agreed to another three years of restrictions following the 15 year extended low-income commitment period and 15 year credit period for a total restriction on the Subject Property of 33 years.<sup>78</sup>

The Subject Property was constructed as a new low-income building, and thus the eligible basis was determined through the adjusted basis, or cost to build the Subject Property plus any capital investments prior to the close of the first taxable year of the credit period.<sup>79</sup> The LURA states that the qualified basis of the Subject Property is \$472,600 while the basis is \$500,000.<sup>80</sup> Because the qualified basis is determined by the applicable fraction of the adjusted basis for the Subject Property, and the qualified basis does not equal the basis, it is apparent that at the time of the addendum either: (1) the adjusted basis was different than the basis; (2) the applicable fraction was less than 1; or (3) some combination of (1) and (2). Common areas are included in the calculation of the floor space fraction,<sup>81</sup> and because there are only 10 units on the Subject Property any unit fraction must be represented by a factor of ten.

The qualified basis of the Subject Property is 95% of the adjusted basis.<sup>82</sup> This indicates one of three possibilities: (1) the unit fraction was 95/100, or nine and one-half of the 10 units are low-income units, which is not possible since the statutes do not contemplate portions of a unit being used as a low-income unit; (2) the floor area fraction was 95/100 which would contemplate that there is some portion of the Subject Property that is not either low-income units or common area associated with the same use, which is not supported by the evidence; or (3) 5% of the basis is not considered applicable to the adjusted basis, which is possible since the portion of the basis associated with the acquisition of land for the low-income project is excluded from the calculation of the qualified basis.<sup>83</sup> The Commission finds that the difference between the qualified basis and the adjusted basis is attributable to the acquisition costs of the land associated with the Subject Property, therefore, at the close of the first taxable year of the tax credit period all of the units of the Subject Property were low-income units.

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<sup>78</sup> *Id.*

<sup>79</sup> 26 U.S.C. §42 (c)(1)(B).

<sup>80</sup> See, E3:149.

<sup>81</sup> See, 26 U.S.C. §42 (d)(4)(B).

<sup>82</sup>  $472,000/500,000 = .95$ .

<sup>83</sup> See, 26 U.S.C. §42 (c)(1)(A) (stating that the qualified basis is determined for “low-income building”).

The addendum to the LURA in 1993 requires the Taxpayer, and any successors, to maintain the same applicable fraction for all 33 years of the LURA. The Subject Property must maintain all 10 units as low-income units. Any calculation of the actual value through the income approach should limit the applicable rental rates to the lesser of the maximum restricted rents for tenants at 60% of the median income, and the market rents.<sup>84</sup>

### **3. Cost Approach and Sales Comparison Approach Opinions of Value**

Kubert conducted sales comparison approach and cost approach determinations of value for the Subject Property as though unencumbered. Kubert used six alleged comparable sales in his sales comparison approach,<sup>85</sup> made adjustments based on several factors,<sup>86</sup> and derived a reconciled sales comparison approach opinion of value of \$600,000.<sup>87</sup> Kubert conducted a cost approach using Marshall & Swift costing tables<sup>88</sup> and an age life depreciation calculation,<sup>89</sup> and derived the land value from eleven sales of properties within Lincoln, Nebraska.<sup>90</sup>

Kubert's sales comparison approach is not based on truly comparable properties. Comparable properties share similar uses (residential, commercial industrial, or agricultural), physical characteristics (size, shape, and topography), and locations.<sup>91</sup> Kubert's alleged comparable properties share some similarities with the Subject Property, and Kubert made adjustments for some of the differences, however, all of the alleged comparable properties consist of at least twice as many units and are multi-story apartment complexes.<sup>92</sup> The Commission gives the sales comparison approach little weight without adjustments for these differences in the characteristics of the alleged comparable properties and the Subject Property.

The Commission also considered Kubert's cost approach. Kubert's appraisal report indicates that the Subject Property has calculable depreciation, and a replacement cost new that can be constructed using accepted appraisal principles and resources. Kubert specified that the cost approach was a valuation of the Subject Property without encumbrances, however, there was

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<sup>84</sup> See, 350 Neb. Admin. Code, Ch. 51 §005.04A (3/09).

<sup>85</sup> See, E3:88-93.

<sup>86</sup> See, E3:97.

<sup>87</sup> See, E3:100.

<sup>88</sup> See, E3:84.

<sup>89</sup> See, E3:85.

<sup>90</sup> See, E3:72-83.

<sup>91</sup> See generally, International Association of Assessing Officers, *Property Assessment Valuation*, at 169-79 (3rd ed. 2010).

<sup>92</sup> See, E3:88-93.

little evidence of any economic obsolescence that would be associated with the encumbrances, and evidence that the expenses for the Subject Property and other low-income projects are high because law requires regular maintenance and upkeep that may also decrease the amount of applicable depreciation.

Nebraska law requires the determination of the actual value of the Subject Property derived for ad valorem tax purposes to take into account the benefits and limitations associated with the Subject Property's involvement in the Section 42 program.<sup>93</sup> Kubert's opinions of value based upon the unencumbered value of the Subject Property do not reflect the benefits and limitations associated with the Subject Property's rights of use under the LURA and as a participating property in the Section 42 program. The Commission gives Kubert's unencumbered sales comparison and cost approach little weight because they do not appropriately take into consideration these important legal characteristics of the Subject Property.

#### **4. Income Approach Opinion of Value**

##### **a. Calculating the PGI**

Kubert conducted an income approach discounted cash flow analysis (DCF).<sup>94</sup> The DCF assumed that the total amount of tax credits was \$35,000.<sup>95</sup> Testimony at the hearing indicated that the actual amount of tax credits was \$350,430 spread out over ten years. Additionally, in his analysis, Kubert extended the value of the tax credits out past the credit period.<sup>96</sup> The tax credits for the Subject Property were accumulated and distributed through year 10 of the project, although the restrictions remain until year 33 under the LURA. Kubert also included the tax credits as income, which is not permissible for an income approach derived by the county assessor for ad valorem tax purposes.<sup>97</sup> The Commission gives Kubert's DCF analysis little weight because it does not conform to Nebraska law and is based in part on incorrect information.

Kubert asserted that the Nebraska Department of Revenue's Rules and Regulations do not allow the use of a DCF to determine the actual value of a rent-restricted property. However,

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<sup>93</sup> See generally, 350 Neb. Admin. Code, Ch. 51 (3/09).

<sup>94</sup> See, E3:130-133.

<sup>95</sup> See, E3:130.

<sup>96</sup> See, E3:130.

<sup>97</sup> See, Neb. Rev. Stat. §77-1333 (Reissue 2009).

Nebraska Statutes permit the use of any professionally accepted mass appraisal method, including a DCF.<sup>98</sup> The statutes, however, do not allow for the tax credits to be considered as income.<sup>99</sup> The Department of Revenue's Rules and Regulations provide guidance for using the different appraisal methods when determining the assessed value of a rent-restricted property.<sup>100</sup> The Commission does not interpret a lack of guidance by the Department of Revenue in its Rules and Regulations as a statement that a DCF could not be used to value a rent-restricted property so long as the appropriate jurisdictional exception is taken by the appraiser and the DCF otherwise comports with Nebraska law.

Additionally, there is insufficient data for the Commission to conduct a direct capitalization income approach for the Subject Property. The development of the potential gross income (PGI) is dependent upon an appropriate selection of the rental rates for the Subject Property. As previously discussed, all units in the Subject Property are rent-restricted under the 1993 addendum to the LURA. Rules and Regulations adopted by the Nebraska Department of Revenue establish that rent for Section 42 rent-restricted units should not include the allowance for utilities.<sup>101</sup> Contract rent, economic rent or market rent, and Maximum Restricted Rent, are terms of art in the assessment of Section 42 rent-restricted property in Nebraska.<sup>102</sup>

Contract rent, also known as actual rent, is the rent actually received for the units at any given time.<sup>103</sup> Economic rent or market rent is the amount of rent a property would receive on the open market for non-restricted units.<sup>104</sup> "Maximum restricted rent is the maximum rent allowed to be collected on housing units subject to the applicable restrictions."<sup>105</sup> Maximum restricted rent may be different for each rent-restricted property, and depends upon the unique target levels contained in the LURA for each property and the median incomes published by HUD.<sup>106</sup>

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<sup>98</sup> See, Neb. Rev. Stat. §77-1333(1).

<sup>99</sup> See, Neb. Rev. Stat. §77-1333(1).

<sup>100</sup> See, 350 Neb. Admin. Code, Ch. 51 §001.01 (3/09).

<sup>101</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01A(6) (3/09).

<sup>102</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 E, F, G, and H (3/09).

<sup>103</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 E; See also, 350 Neb. Admin. Code, Ch. 51 §004.06C (3/09).

<sup>104</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 F; See also, 350 Neb. Admin. Code, Ch. 51 §004.06A (3/09).

<sup>105</sup> See 350 Neb. Admin. Code, Ch. 51 §002.01 H (3/09); See also, 350 Neb. Admin. Code, Ch. 51 §004.06B (3/09).

<sup>106</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 H (3/09); See also, 350 Neb. Admin. Code, Ch. 51 §004.06B (3/09).

When an assessor or appraiser uses the income approach to value a rent-restricted property the potential gross income (PGI) should be calculated “using the lesser of market rent or the Maximum Restricted Rent[.]”<sup>107</sup>

Kubert utilized the contract rents, and asserted that this was the best practice because “most units [are] occupied by less than the maximum tenant mix resulting in reduced income and subsequent rent. In addition, a majority of the units include housing assistance from the Lincoln Housing Authority which establishes the maximum rent.”<sup>108</sup> Neither the LURA, Nebraska Law, nor the United States Code requires that the units be occupied by tenants receiving housing assistance. The LURA indicates that the Taxpayer cannot discriminate against prospective tenants who receive housing assistance and those who do not, and must make determinations based upon income.<sup>109</sup> In fact, because all of the units are rent-restricted or low-income units under the 1993 addendum to the LURA, the Taxpayer must collect income information from each prospective tenant and make determinations based on income.

The evidence indicated that the Subject Property is occupied by Qualified Tenants whose income is below the maximum allowable income. The Department of Revenue’s Rules and Regulations also allow the use of a normalized operating history to support the calculation of the net operating income (NOI).<sup>110</sup> However, the normalized operating history alone is insufficient because it may be affected by management decisions that vary from typical management decisions at comparable properties. In this case, Medina testified, and the LURA suggests, that the tenant mix of the Subject Property has been the result of management decisions. These management decisions affect the normalized operating history and, therefore, affect the credibility of an opinion of value based on the normalized operating history without supporting data from other comparable rent-restricted properties indicating that the normalized operating history is similar to the other comparable rent-restricted properties. It is inappropriate to use contract rents to determine the PGI of the Subject Property because there is not sufficient evidence that the Subject Property only attracts tenants whose income is well below the maximum allowable income.

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<sup>107</sup> 350 Neb. Admin. Code, Ch. 51 §005.04A (3/09).

<sup>108</sup> E3:122. Such housing assistance is in the form of a rental subsidy.

<sup>109</sup> See, E3:157.

<sup>110</sup> See, 350 Neb. Admin. Code, Ch. 51 §005.04D (3/09).



There is not sufficient evidence to indicate whether or not multiple markets exist within the Section 42 LIHTC property market in Lincoln, Nebraska. There is also insufficient evidence to indicate that a sub-market exists where all low-income projects are restricted to 60% income limitations, but where all tenants have income well below the maximum income limitation. The Taxpayer's assertion that rents from other Section 42 properties should be examined to determine the applicable rental rate relies on the preceding theoretical conditions. However, insufficient evidence was presented to establish that these theoretical market conditions actually exist.

Medina testified that the Subject Property is allowed by the LURA and by Section 42 to charge rents in excess of the current contract rents. However, Medina testified that the Subject Property charges rents that are comparable to other rent-restricted properties, and that a knowledgeable prospective tenant could find and compare the Subject Property's rental rates and rental rates from other similar rent-restricted properties. Medina provided a list of alleged comparable properties that she asserted were obtained from a government listing service providing the public with access to rent-restricted unit listings.<sup>111</sup> Medina's list of alleged comparable properties provides rents for two bedroom apartments of \$705, \$697, and \$675.<sup>112</sup> Medina's list of alleged comparable properties provides rents for three bedroom apartments of \$845, \$825, \$785, \$749, and \$695.<sup>113</sup>

Medina did not testify concerning the physical characteristics of the alleged comparable properties. She also did not testify concerning their proximity to the Subject Property. The listing of comparable properties is insufficient evidence to support the assertion that the Subject Property operates in a specific sub-market of lower income low-income units without the property record cards for the comparable properties and more evidence of the comparable properties' physical characteristics.

If sufficient evidence had been adduced indicating that the Subject Property operated and competed in a limited market of tenants receiving housing assistance, then the market rents would need to reflect that limitation. However, based upon the evidence received in the current appeal, it is inappropriate to use contract rents to determine the PGI of the Subject Property.

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<sup>111</sup> See, E22:2.

<sup>112</sup> See, E22:2.

<sup>113</sup> See, E22:2.

Kubert provided the market rents for the Subject Property, or the amount the units for the Subject Property would command on the open market without rent restrictions.<sup>114</sup> Kubert provided ten alleged comparable properties and their contract rents.<sup>115</sup> He also indicated that these properties were located in the same general area as the Subject Property.<sup>116</sup> Comparable properties share similar uses (residential, commercial/industrial, or agricultural), physical characteristics (size, shape, and topography), and locations.<sup>117</sup> The evidence indicates that the Subject Property and Kubert's comparable properties share similar residential uses and locations. However, the evidence also indicates that there are significant differences between the physical characteristics of Kubert's comparable properties and the physical characteristics of the Subject Property. Specifically, all of Kubert's alleged comparable properties consist of multi-story apartment complexes with surface parking.<sup>118</sup> The Subject Property consists of five duplexes, some featuring garages.<sup>119</sup>

Because of these differences, the Subject Property and Kubert's alleged comparable properties are not comparable. Therefore, Kubert's market rents are not indicative of the rent the Subject Property would bring on the open market without rent restrictions. Kubert's market rents should not be used to determine the Subject Property's PGI, and no other estimation of the market rent is in evidence. Applying the Department of Revenue's Rules and Regulations to the evidence in this appeal, the only remaining type of rent that may be used to calculate the PGI is the maximum restricted rent.<sup>120</sup>

However, the maximum restricted rent calculation is also unavailable to the Commission.<sup>121</sup> Kubert reported that the 2011 maximum rent for a two bedroom unit was \$943 and the maximum restricted rent for a three bedroom unit was \$1,089.<sup>122</sup> These figures include the utility allowance which must be subtracted from the determination of the maximum rent.<sup>123</sup> The evidence does not include the utility allowances applicable as of January 1, 2012. The

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<sup>114</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01 F; See also, 350 Neb. Admin. Code, Ch. 51 §004.06A (3/09).

<sup>115</sup> See, E3:103-112.

<sup>116</sup> See, E3:113 (map of alleged comparable properties and the Subject Property).

<sup>117</sup> See generally, International Association of Assessing Officers, *Property Assessment Valuation*, at 169-79 (3rd ed. 2010).

<sup>118</sup> See, E3:103-112.

<sup>119</sup> See, E2:6-12.

<sup>120</sup> See, 350 Neb. Admin. Code, Ch. 51 §005.04A (3/09).

<sup>121</sup> See, E3:121.

<sup>122</sup> *Id.*

<sup>123</sup> See, 350 Neb. Admin. Code, Ch. 51 §002.01A(6) (3/09).

Taxpayer's exhibits include the utility allowances applicable as of January 1, 2014.<sup>124</sup> The 2014 utility allowances are \$136 for two-bedroom duplex units and \$161 for three-bedroom duplex units.<sup>125</sup> This results in a total maximum restricted rent of \$807 for two-bedroom units and \$928 for three-bedroom units. However, without the applicable utility allowances for 2012, the Commission is unable to determine a PGI that conforms with Nebraska Law.

#### **b. Actual Value of the Subject Property**

The Department of Revenue's Rules and Regulations require that when calculating the PGI in a direct capitalization income approach for a rent-restricted property the lesser of the market rent and the maximum restricted rent should be used. Market rents for the Subject Property are not known; the Taxpayer did not provide sufficient evidence to establish that a market exists within the low-income housing market in Lincoln, Nebraska where the only applicants are those who qualify for rental subsidies, and the market rent derived in Kubert's appraisal report is based on properties that are not comparable to the Subject Property. Further, the maximum restricted rent is not determinable. For these reasons, the Commission cannot determine which is the lesser value, the market rent or the maximum restricted rent. Again, the operating history for the Subject Property is not dispositive because there is evidence that the historical and current tenant mix may be the result of management decisions and not representative of the market.

The Commission finds that the actual value of the Subject Property cannot be derived from the evidence, even though multiple opinions were presented. Because there is not sufficient evidence of an appropriate alternative opinion of actual value, and there is no evidence that the County Board's determination was based on incorrect calculations or methods, the Commission finds that there is not clear and convincing evidence that the County Board's determination was arbitrary or unreasonable. The Commission finds that it is possible that the market rental rates may produce an opinion of value lower than the actual value determined through use of the maximum restricted rent. However, the Commission is limited to the evidence, and there is not clear and convincing evidence that the County Board's determination was arbitrary or unreasonable. Therefore, the County Board's determination of value should be affirmed.

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<sup>124</sup> See, E22:4.

<sup>125</sup> *Id.*

## V. CONCLUSION

The Commission finds that there is competent evidence to rebut the presumption that the County Board faithfully performed its duties and had sufficient competent evidence to make its determination. However, the Commission also finds that there is not clear and convincing evidence that the County Board's decision was arbitrary or unreasonable.

For all of the reasons set forth above, the determination by the County Board is affirmed.

## VI. ORDER

IT IS ORDERED THAT:

1. The decision of the Lancaster County Board of Equalization determining the value of the Subject Property for tax year 2012 is affirmed.<sup>126</sup>
2. The taxable value of the Subject Property for tax year 2012 is \$594,900.
3. This Decision and Order, if no appeal is timely filed, shall be certified to the Lancaster County Treasurer and the Lancaster County Assessor, pursuant to Neb. Rev. Stat. §77-5018 (2012 Cum. Supp.).
4. Any request for relief, by any party, which is not specifically provided for by this Decision and Order is denied.
5. Each party is to bear its own costs in this proceeding.
6. This Decision and Order shall only be applicable to tax year 2012.
7. This Decision and Order is effective for purposes of appeal on December 2, 2014.<sup>127</sup>

Signed and Sealed: December 2, 2014.

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Robert W. Hotz, Commissioner

SEAL

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Nancy J. Salmon, Commissioner

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<sup>126</sup> Assessed value, as determined by the County Board, was based upon the evidence at the time of the Protest proceeding. At the appeal hearing before the Commission, both parties were permitted to submit evidence that may not have been considered by the County Board of Equalization at the protest proceeding.

<sup>127</sup> Appeals from any decision of the Commission must satisfy the requirements of Neb. Rev. Stat. §77-5019 (2012 Cum. Supp.) and other provisions of Nebraska Statutes and Court Rules.