BEFORE THE NEBRASKA TAX EQUALIZATION AND REVIEW COMMISSION

The Orchards at Wildewood, LP., Appellant, v. Sarpy County Board of Equalization, Appellee.	Case Nos: 12C 003, 13C 020, & 14C 139 Decision and Order Reversing the Determinations of the Sarpy County Board of Equalization

For the Appellant:
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For the Appellee:
Michael A. Smith,
Deputy Sarpy County Attorney.

These appeals were heard before Commissioners Robert W. Hotz and Nancy J. Salmon.

I. THE SUBJECT PROPERTY

The Subject Property is a commercial parcel located at 7454 Gertrude Street, Papillion, Sarpy County, Nebraska. The parcel is improved with rent-restricted housing that receives low-income housing tax credits (LIHTC). The legal description of the Subject Property is found at Exhibit 1. The property record cards for the Subject Property are found at Exhibits 4 through 6.

II. PROCEDURAL HISTORY

The Sarpy County Assessor (the Assessor) determined that the assessed value of the Subject Property was $2,150,000 for tax year 2012. The Orchards at Wildewood, LP. (the Taxpayer) protested this assessment to the Sarpy County Board of Equalization (the County Board). The County Board determined that the taxable value for tax year 2012 was $2,030,000.[1]

The Assessor determined that the assessed value of the Subject Property was $2,530,000 for tax year 2013. The Taxpayer protested this assessment to the County Board. The County Board determined that the taxable value for tax year 2013 was $2,530,000.[2]

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[1] See, E1.
[2] See, E2.

The Assessor determined that the assessed value of the Subject Property was $2,530,000 for tax year 2014. The Taxpayer protested this assessment to the County Board. The County Board determined that the taxable value for tax year 2014 was $2,530,000.[3]

The Taxpayer appealed the decisions of the County Board to the Tax Equalization and Review Commission (the 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 February 12, 2015.

III. STANDARD OF REVIEW

The Commission's review of the determination by a County Board of Equalization is de novo.[4] 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."[5]

> 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.[6]

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.[7] Proof that the order, decision, determination, or action was unreasonable or arbitrary must be made by clear and convincing evidence.[8]

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[3] See, E3.
[4] See, Neb. Rev. Stat. §77-5016(8) (2014 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).
[5] *Brenner v. Banner Cty. Bd. Of Equal*., 276 Neb. 275, 283, 753 N.W.2d 802, 811 (2008) (Citations omitted).
[6] *Id.*
[7] Neb. Rev. Stat. §77-5016(8) (2014 Cum. Supp.).
[8] *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.[9] 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.[10]

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."[11] 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."[12] The Commission's Decision and Order shall include findings of fact and conclusions of law.[13]

IV. VALUATION

A. Law

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.[14]

"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."[15] "Actual value, market value, and fair market value mean exactly the same thing."[16] Taxable value is the percentage of actual value

[9] 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).
[10] *Bottorf v. Clay County Bd. of Equalization,* 7 Neb.App. 162, 580 N.W.2d 561 (1998).
[11] Neb. Rev. Stat. §77-5016(8) (2014 Cum. Supp.).
[12] Neb. Rev. Stat. §77-5016(6) (2014 Cum. Supp.).
[13] Neb. Rev. Stat. §77-5018(1) (2014 Cum. Supp.).
[14] Neb. Rev. Stat. §77-112 (Reissue 2009).
[15] *Id*.
[16] *Omaha Country Club v. Douglas County Board of Equalization, et al.*, 11 Neb.App. 171, 180, 645 N.W.2d 821, 829 (2002).

subject to taxation as directed by section 77-201 of Nebraska Statutes and has the same meaning as assessed value.[17] All real property in Nebraska subject to taxation shall be assessed as of January 1.[18] All taxable real property, with the exception of agricultural land and horticultural land, shall be valued at actual value for purposes of taxation.[19]

B. Low-Income Housing Tax Credit (LIHTC) Program[20]

Nebraska Statutes require county assessors to perform an income approach calculation for all rent-restricted housing projects and prohibit county assessors from including as income in this calculation any tax credits received.[21] Such tax credits may be considered when determining the capitalization rate when capitalizing the income stream.[22] 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.[23] Specifically, rent for rent-restricted units should not include the allowance for utilities.[24] Contract rent, economic rent or market rent, Fair Market Rent (FMR), and Maximum Restricted Rent, are terms of art in the assessment of rent-restricted property.[25]

Contract rent, also known as actual rent, is the rent actually received for the units at any given time.[26] Economic rent or market rent is the amount of rent a property would receive on the open market for non-restricted units.[27] FMR is a term that describes "the maximum rent allowed to be collected on housing units subject to federal subsidy payments."[28] 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 not included in the preceding three areas.[29] FMR is published annually.[30] Maximum restricted rent is "the maximum rent allowed

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[17] Neb. Rev. Stat. §77-131 (Reissue 2009).
[18] See, Neb. Rev. Stat. §77-1301(1) (Reissue 2009).
[19] Neb. Rev. Stat. §77-201(1) (Reissue 2009).
[20] See, I.R.C. §42
[21] See, Neb. Rev. Stat. §77-1333 (Reissue 2009). The requirement to perform an income approach calculation for all rent-restricted housing projects 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).
[22] See, Neb. Rev. Stat. §77-1333 (Reissue 2009).
[23] See, 350 Neb. Admin. Code, Ch. 51 (3/09).
[24] See, 350 Neb. Admin. Code, Ch. 51 §002.01A(6) (3/09).
[25] See, 350 Neb. Admin. Code, Ch. 51 §002.01 E, F, G, and H (3/09).
[26] See, 350 Neb. Admin. Code, Ch. 51 §002.01 E; See also, 350 Neb. Admin. Code, Ch. 51 §004.06C (3/09).
[27] See, 350 Neb. Admin. Code, Ch. 51 §002.01 F; See also, 350 Neb. Admin. Code, Ch. 51 §004.06A (3/09).
[28] See, 350 Neb. Admin. Code, Ch. 51 §002.01 G (3/09).
[29] See, 350 Neb. Admin. Code, Ch. 51 §002.01 G (3/09).
[30] See, 350 Neb. Admin. Code, Ch. 51 §002.01 G (3/09).

to be collected on housing units subject to the applicable restrictions."[31] Maximum restricted rent may be different for each rent-restricted property, and depends upon the unique target levels contained in the land use restriction agreement (LURA) for each property and the median incomes published by HUD.[32]

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.[33] 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[.]"[34] When determining the capitalization rate, the assessor or appraiser must consider the tax credits, rental rates, and restrictions using generally accepted appraisal methods.[35]

C. Summary of the Evidence

At all relevant times pertinent to these appeals, the owner of the Subject Property was The Orchards at Wildewood, LP. William Truax, secretary of the sole owning entity of the general partner in The Orchards at Wildewood, LP, testified that the Subject Property was restricted by a land use restriction agreement (LURA) that restricted both the income of the tenants and the age of the tenants. Specifically, the Subject Property was restricted to tenants who met income qualifications and were over 55 years of age.[36] He testified that the project was funded by: (1) syndicators who became limited partners; (2) a mortgage on the property;[37] (3) a federal grant secured against the real property with potential recapture;[38] and (4) a developer's fee.[39]

Truax testified that the Subject Property was fully constructed and all units were placed in service by 2012, but that the Subject Property was not fully occupied until later. He asserted that the actual vacancy and collection loss rates for the Subject Property were 18.8% for 2012, 8% for

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[31] 350 Neb. Admin. Code, Ch. 51 §002.01 H (3/09); See also, 350 Neb. Admin. Code, Ch. 51 §004.06B (3/09).
[32] See, 350 Neb. Admin. Code, Ch. 51 §002.01 H (3/09); See also, 350 Neb. Admin. Code, Ch. 51 §004.06B (3/09).
[33] See, 350 Neb. Admin. Code, Ch. 51 §005 (3/09).
[34] 350 Neb. Admin. Code, Ch. 51 §005.04A (3/09).
[35] 350 Neb. Admin. Code, Ch. 51 §005.04E (3/09).
[36] See, E20:18-39.
[37] See, E20:118.
[38] See, E20:118. Truax testified that the federal grant was distributed over 15 years and that if recapture occurred there would be no interest.
[39] See, E20:113. Truax testified that the developer's fee may never by fully paid.

2013, and 2.1% for 2014. He also asserted that LIHTC properties experience higher expenses than other properties and asserted the Subject Property's actual expenses were 52% for tax year 2012, 52% for 2013, and 54% for 2014.

Truax asserted that the tax credits associated with the Subject Property were items of intangible property and that the value of the tax credits should not be considered when determining the value of the Subject Property. Specifically, Truax asserted that not only should the value associated with the tax credits be excluded from the calculation of the net operating income (NOI), but that the tax credits should be excluded from the determination of the capitalization rate.

Despite these assertions, Truax testified that the sale of the tax credits to the limited partners resulted in $4,501,459 of equity in the Subject Property and that part of the developer's fee owed to the general partner had yet to be repaid.

Brad Weinberg[40] conducted appraisals of the Subject Property. He received two separate appraisal assignments. The first assignment was for retroactive appraisals as of January 1, 2012, and January 1, 2013.[41] The second assignment was for retroactive appraisals as of January 1, 2012, January 1, 2013, and January 1, 2014.[42] At the hearing, Weinberg relied upon the second set of retroactive appraisals for his opinions of value.

Weinberg appraised the Subject Property using the income approach. Weinberg testified that the most important consideration when appraising an LIHTC property was the LURA. He asserted that he derived his NOI using the maximum restricted rents, as defined by the Department of Revenue, because the maximum restricted rents were below the market rents for unrestricted properties. Weinberg testified that due to the nature of his employment he had access to the actual expenses of nearly 1,500 comparable properties to derive the expense ratio he used in his appraisals.

Weinberg also asserted that tax credits are intangible property and that they should not be considered when determining the actual value of LIHTC properties. Weinberg testified that

[40] Weinberg is an MIA designated real estate appraiser, licensed in multiple jurisdictions. See, E22:122-123 (Curriculum Vitae).
[41] See, E20:134-251.
[42] See, E24.

because Nebraska law allows the tax credits to be considered in the capitalization rate he performed a discounted tax flow analysis considering the tax credits. He asserted that he utilized a yield ratio of 11.5%. He testified that his derived capitalization rate, when accounting for the tax credits, derived a higher capitalization rate than his market capitalization rate. Weinberg also asserted that this was typical of calculated capitalization rates with other LIHTC properties, and that part of the reason that he excludes the tax credits from a determination of the capitalization rate is that it invariably results in a higher capitalization rate, which, he said, is contrary to logic since LIHTC properties benefit from low debt to equity ratio.

In his first appraisals, Weinberg used capitalization rates derived from unrestricted apartment buildings to determine the actual value of the Subject Property using a band of investment method, a debt coverage ratio method, and a market extraction method.[43] In his second appraisals, he used a market extraction method for deriving the overall capitalization rate based upon sales of unrestricted apartment complexes.[44] There is no evidence that Weinberg conducted a band of investment method or debt coverage ratio method when determining the capitalization rates and taking into account the right to receive tax credits. While Weinberg considered using the tax credits in his appraisals, he did not actually use the tax credits in his calculated NOI or capitalization rate.[45] Weinberg asserted that the use of tax credits in any calculation of the actual value was inappropriate and contrary to Uniform Standards of Professional Appraisal Practice (USPAP), which he asserted consider the tax credits intangible property.

Tim Ederer, an employee of the Sarpy County Assessor, testified that the Subject Property was valued using the income approach and that he had relied upon market factors derived from unrestricted properties.[46] He asserted that the Subject Property was required to be valued at its actual value, and that he was required to assess the fee simple interest of the Subject Property. He asserted that under the bundle of rights theory, the government had purchased some of the rights associated with the Subject Property as expressed in the LURA. He asserted that by valuing the Subject Property as though it were unrestricted, he was valuing the fee simple

[43] See, E20:202-207.
[44] See, E24:67-70.
[45] See, E20:202 and E24:67
[46] See, E4, E5, and E6.

interest in the Subject Property instead of only the leased fee interest in the Subject Property. He asserted that he derived the capitalization rate through a band of investment method using market data,[47] and that he had used market rents instead of maximum restricted rents even though the market rents were higher than the maximum restricted rents.

D. Summary & Analysis

The Taxpayer's and County Board's assertions are summarized as three distinct issues: (1) are low-income housing tax credits intangible personal property that cannot be considered in determining the actual value of the Subject Property for ad valorem tax purposes; (2) does Nebraska law require the assessment of the fee simple interest of the Subject Property; and (3) what is the actual value of the Subject Property? The Commission takes up these issues separately below and finds that: (1) low-income housing tax credits are "part of the economic reality" of the Subject Property and may be considered in determining the actual value of the Subject Property; (2) Nebraska law requires the assessment of the fee simple interest of the Subject Property; and (3) the County Board's determinations are arbitrary or unreasonable.

1. Intangible Property v. Real Property

Nebraska law defines real property as:

> (1) All land;
> (2) All buildings, improvements, and fixtures, except trade fixtures;
> …
> (5) All privileges pertaining to real property described in subdivisions (1) through (4) of this section.[48]

Nebraska statutes define intangible property as personal property that is not defined as tangible personal property, including money.[49] Tangible personal property is defined as "personal property possessing a physical existence, excluding money."[50]

The Nebraska Supreme Court has considered the use of tax credits in determining the assessed value of real property.[51] The Nebraska Supreme Court has accepted as consistent with

[47] See, E13.
[48] Neb. Rev. Stat. §77-103 (Reissue 2009).
[49] Neb. Rev. Stat. §77-105 (2014 Cum. Supp.).
[50] Neb. Rev. Stat. §77-105 (2014 Cum. Supp.).

Nebraska Statute the proposition that "credits are part of the economic reality of the property[.]"[52] The Taxpayer asserted that this position is contrary to USPAP.[53] USPAP does not trump Nebraska law regarding the assessment of real property in Nebraska. While USPAP treats LIHTC tax credits as intangible personal property not to be included as real property, it is not the intangible tax credits that are valued in an income approach but rather the value of the right to access the tax credits by an entity with an ownership interest in the real property.

The assessed value of the Subject Property should be based solely on the actual value of the real property.[54] Money is intangible personal property.[55] All of the commonly accepted appraisal techniques express the actual value of real property in terms of the amount of money which a willing seller could expect to receive from a willing buyer in an arm's length transaction for the real property. Moreover, when deriving the actual value of real property, each approach considers either: (1) the amount of money that has been received in consideration for real property;[56] (2) the amount of money needed to purchase the services, tangible personal property, or lots necessary to create a property;[57] or (3) the amount of money in income that an owner could expect to derive from all income producing activities of the real property capitalized over its expected life.[58] Thus, while the actual value of intangible personal property should not be included in a determination of the actual value of real property, it is requisite that the actual value of the real property is expressed by a quantified amount of intangible personal property that would be exchanged for the real property on the open market. In order to derive the actual value of real property, the assessing or appraising individual must consider that amount of intangible personal property that expresses the contributing value of various real property rights. This is consistent with Nebraska law and professionally accepted appraisal techniques.

Other jurisdictions also accept this position.[59] A Georgia appellate court rejected assertions that tax credits were intangible property and found that equity investments from limited partners

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[51] See, *Schuyler Apartment Partners, LLC v. Colfax County Bd. Of Equalization*, 279 Neb. 989, 783 N.W.2d 587 (2010).
[52] *Id*. at 995, 783 N.W.2d at 592.
[53] USPAP Advisory Opinion 14.
[54] Neb. Rev. Stat. §77-112 (Reissue 2009).
[55] Neb. Rev. Stat. §77-105 (2014 Cum. Supp.).
[56] See, Appraisal Institute, *The Appraisal of Real Estate*, at 381-82 (14th ed. 2013).
[57] See, International Association of Assessing Officers, *Property Assessment Valuation*, at 230 (3rd ed. 2010).
[58] See, Appraisal Institute, *The Dictionary of Real Estate Appraisal*, at143 (4th ed. 2002).
[59] See, *Huron Ridge LP, v. Ypsilanti Township*, 275 Mich.App. 23, 737 N.W.2d 187 (Mich.App. 2007) (holding that §42 tax credits must be considered when determining the value of real property for tax purposes); *Parkside Townhomes Assoc. v. Bd. Of Assessment Appeals of York County*, 711 A.2d 607 (PaCommwCT 1998); *Brandon Bay, Limited Partnership, v. Payette County*,

in return for an ownership interest in an LIHTC project and access to tax credits is a "stream of value tied solely to the property[.]"[60] The tax credits can only be claimed by entities with an ownership interest in the real property.[61] As the California Court of Appeal, First District, Second Division, succinctly noted:

> It is true that certain references to an LIHTC [a low-income housing tax credit] being "sold" can be found in reported decisions. But this is misleading unless substantially qualified. A person or entity cannot be allocated an LIHTC and immediately sell it on any street corner. The housing project must be completed and made operational before the credits begin to appear on a tax return. Thereafter, the project may be sold, but the LIHTC is transferred with the property; the LIHTC cannot be sold separately.[62]

The Commission finds that it is appropriate to consider the amount of money expended by investors to purchase an ownership interest in an LIHTC property when determining the actual value of the Subject Property for assessment purposes. The Commission also finds that the tax credits are a privilege associated with improvements and land comprising the Subject Property and that privilege is defined as real property under Nebraska law.[63]

The federal government provides the tax credits in consideration for the rights it obtains and the restrictions that are put in place in the LURA.[64] The testimony in the hearing indicates that investors purchase an ownership interest in the limited partnership owning the LIHTC property. The limited partners are then able to utilize the tax credits to offset federal income tax liabilities. The amount limited partners are required to pay to obtain an ownership interest in the limited

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142 Idaho 681, 685, 132 P.3d 438, 441 (Idaho 2006) ("Because the tax credits are rights and privileges that directly relate to the real estate, they are properly considered in assessing the value of low-income housing"); *Town Square Ltd. P'ship v. Clay County Bd. Of Equalization*, 704 N.W.2d 896 (S.D. 2005); *Pine Pont Housing LP v. Lowndes County Bd of Tax Assessors*, 254 Ga.App. 197, 561 S.E.2d 860 (2002) (holding that tax credits were associated with the real property and should be considered when determining fair market value); *In re Ottwa Housing Assoc., L.P.*, 10 P.3d 777 (Kan.App. 2000) (holding that the effect of tax credits and rent restrictions should be taken into account when valuing LIHTC properties); *Pedcor Investments – 1990-XIII, L.P., v. State Bd. Of Tax Com'rs*, 715 N.E.2d 432 (Ind. Tax 1999) (affirming a lower tribunals reasoning that LIHTC could be considered when determining the fair market value of real property for tax purposes); *Alta Pacific v. Utah State Tax Com'n*, 931 P.2d 103 (Utah 1997) (holding that it was appropriate to consider the decreased risk associated with LIHTC properties when determining fair market value); *Rebelwood, LTD, v. Hinds County*, 544 So.2d 1365, (Miss. 1989) (holding "benefits enjoyed by Taxpayer by reason of its ownership of Rebelwood must be considered in establishing true value for each year in which such subsidy or benefits are in fact enjoyed"); and *Steele v. Town of Allenstown*, 471 A.2d 1179, 124 N.H. 487 (1984) (holding that federal subsidies for LIHTC housing should be considered in determining the fair market value of a project for ad valorem tax purposes).

[60] *Pine Pont Housing LP v. Lowndes County Bd of Tax Assessors*, 254 Ga.App. 197, 200, 561 S.E.2d 860 (2002).

[61] See generally, *Randall v. Loftsgaarden*, 478 U.S. 647, 666, 106 S.Ct. 3143, 3154 (1986) (stating as "obvious" that tax credits are not freely transferable if severed from the property "in the absence of a statutory provision to the contrary[.]"); See also, 26 U.S.C. §42 (d)(7), (f)(1), (4), (5); See also, 26 CFR 1.42-1t(a)(2) (2004) (indicating that Sec. 42 credit is allowed to the extent an owner of the building receives an allocation from a housing credit agency).

[62] *State ex rel. Dockstader v. Hamby*, 162 Cal.App.4th 289, 313 (2008) (citations omitted).

[63] Neb. Rev. Stat. §77-105 (2014 Cum. Supp.).

[64] See, E20:18-99 (LURA).

partnership is derived from the market rate of the amount of tax credits the limited partner expects to access as a partner in the owning entity. The amount paid by partners for the tax credits, which are consideration for the privileges to access tax credits, is simply a way of expressing the value of those privileges to access the tax credits.

Similarly, rents paid for the rights to live in the residential units that comprise the Subject Property are composed of money, or intangible personal property. However, it is appropriate to consider the rent under the income approach when deriving the actual value of the real property. The intangible personal property, money, is simply the uniform method of expressing value in exchange and is therefore a necessary component in deriving the income producing capability of a property.

The Commission finds that including in the income approach a consideration of the amount of money that limited partners pay to obtain an ownership interest in LIHTC property in order to utilize the privileges associated with the real property, specifically the right to use tax credits, is consistent with Nebraska law, so long as that consideration is limited to the development of the capitalization rate applicable for the Subject Property and not as income.

2. Fee Simple Interest vs. a Partial Interest

Ederer testified that he did not use the maximum restricted rents as calculated from the LURA, but instead used market rents.[65] Ederer asserted that he was required to value the fee simple interest of the Subject Property and not the leased fee interest. He asserted that under the bundle of rights theory he considered that the LURA included a delegation of some of the property rights present in the fee simple interest in consideration for tax credits. He asserted that it was inappropriate to ignore higher market rents when deriving the Subject Property's NOI simply because the Subject Property's owner had intentionally sold off a portion of the fee simple interest. Rules and regulations promulgated by the Tax Commissioner require a county assessor to use the lesser of maximum restricted rents or market rents to derive the NOI when using the income approach to determine the taxable value of LIHTC properties in Nebraska.[66] Ederer's assertions imply that the Tax Commissioner's rules and regulations require the

[65] See, E4, E5, and E6.
[66] See, 350 Neb. Admin. Code, Ch. 51 §005.04A (3/09).

assessment of a partial interest of LIHTC properties, but that Nebraska law requires the assessment of the fee simple interest.

A fee simple interest is "the largest estate and most extensive interest that can be enjoyed in land."[67] "Ownership of the fee simple interest is equivalent to ownership of the complete bundle of sticks, while one or more of the sticks (or a portion of individual sticks) can represent a partial interest in a specific property."[68] "Each individual right in the bundle may have potential value. If any or all are removed from the fee simple interest, one or more partial interests are created."[69] "Individual rights can be separated from the bundle by sale, lease, mortgage, donation, or another means of transfer."[70] "A lease conveys property rights from a landlord (lessor) to a tenant (lessee). Fee ownership remains with the landlord, who is said to have a leased fee interest."[71] "The assessor typically values property as an estate in fee simple, unless statute or administrative rules dictate otherwise."[72] "An appraiser may be asked to appraise something less than the fee simple interest – i.e., a partial interest or a fractional interest."[73]

In previous orders concerning LIHTC properties, the Commission has consistently followed the rules and regulations promulgated by the Tax Commissioner regarding the assessment of rent restricted properties.[74] In those cases the issue of the valuation of a fee simple interest versus the valuation of a partial interest was never raised. Here, Ederer's testimony suggests a novel legal argument that requires further attention.

The Commission concurs that the sale of the right to charge market rents over the course of 45 years in consideration for tax credits resulted in a divestment of one of the property rights included in the fee simple interest for the term of the LURA. Additionally, the Commission concurs that the Tax Commissioner's rules and regulations require the assessment of a partial or fractional interest instead of the fee simple interest. However, a separate question is whether Nebraska law required the County to value the fee simple interest.

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[67] See, *Black's Law Dictionary 7th Edition*, West Group, p. 615 (1999) (definition Fee Simple).
[68] See, The Appraisal Institute, *The Appraisal of Real Estate*, at 5 (14th ed. 2013).
[69] See, The Appraisal Institute, *The Appraisal of Real Estate*, at 5 (14th ed. 2013).
[70] See, The Appraisal Institute, *The Appraisal of Real Estate*, at 5 (14th ed. 2013).
[71] See, International Association of Assessing Officers, *Property Assessment Valuation*, at 12 (3rd ed. 2010).
[72] See, International Association of Assessing Officers, *Property Assessment Valuation*, at 12 (3rd ed. 2010).
[73] See, The Appraisal Institute, *The Appraisal of Real Estate*, at 5 (14th ed. 2013).
[74] See, 350 Neb. Admin. Code, ch. 51 (03/15/2009).

General assessment principles state that, "[t]he assessor typically values property as an estate in fee simple, unless statute or administrative rules dictate otherwise."[75] Nebraska law requires the assessor to assess all real property other than agricultural land and horticultural land at actual value:

> Actual value of real property for purposes of taxation means the market value of real property in the ordinary course of trade. Actual value may be determined using professionally accepted mass appraisal methods, including, but not limited to, the (1) sales comparison approach, (2) income approach, and (3) cost approach. Actual 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 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 consideration of the full description of the physical characteristics of the real property and an identification of the property rights being valued.[76]

The Commission finds no specific requirement in statute or rules and regulations that requires the assessment of the fee simple interest instead of a partial interest. However, the Nebraska Court of Appeals has considered whether the statutory requirement that real property be assessed at actual value meant the actual value of the fee simple interest or the actual value of some partial interest maintained by the owner of record in *Omaha Country Club v. Douglas County Board of Equalization*.[77] At issue in *Omaha Country Club* was the then-applicable language of Neb. Rev. Stat. §77-112, which was substantially similar to the law applicable in this appeal, and which read as follows:

> Actual value of real property for purposes of taxation means the market value of real property in the ordinary course of trade. Actual value may be determined using professionally accepted mass appraisal methods, including, but not limited to, the (1) sales comparison approach, (2) income approach, and (3) cost approach.

In *Omaha Country Club*, the taxpayer asserted that long terms leases for amounts substantially below then-current markets should be considered in determining the actual value of the subject property for property tax purposes.[78] The taxpayer appealed a previous Commission determination wherein the Commission held, "actual or fair market value of the real property can

[75] See, International Association of Assessing Officers, *Property Assessment Valuation*, at 12 (3rd ed. 2010).
[76] See, Neb. Rev. Stat. §77-201(1) (2014 Cum. Supp.).
[77] *Omaha Country Club v. Douglas County Board of Equalization*, 11 Neb.App. 171, 645 N.W.2d 822, 824 (2002).
[78] *Omaha Country Club v. Douglas County Board of Equalization*, 11 Neb.App. 171, 645 N.W.2d 822, 824 (2002).

only be ascertained by determining the value of the fee simple estate, including the Leasehold Estate, the Leased Fee Estate, and any severed estates."[79]

The Nebraska Court of Appeals reasoned that the rules and regulations promulgated by the Department of Revenue defined real property to include, "all privileges relating to real property[,]" and that the privileges were defined as "the right to sell, lease, use, give away, or enter and the right to refuse to do any of these. All rights may or may not be vested in one owner or interest holder."[80] The Nebraska Court of Appeals also examined case law from other jurisdictions with similar state laws and held, "that the actual value of real property for tax purposes shall be the value which a willing buyer would be willing to pay for the fee simple interest."[81]

While the reasoning of the Nebraska Court of Appeals in *Omaha Country Club* relied upon previous versions of statute and rules and regulations, the current version of Neb. Rev. Stat. §77-112 is substantially similar to the version examined in the case. The pertinent parts of the rules and regulations examined by the Nebraska Court of Appeals are identical.[82]

Subsequent to *Omaha Country Club,* the Legislature enacted Neb. Rev. Stat. §77-1333, requiring the county assessor to perform an income approach for LIHTC properties and permitting the county assessor to take into account the tax credits when deriving the capitalization rate.[83] The legislature required that, "[t]he income-approach calculation shall be consistent with any rules and regulations adopted and promulgated by the Tax Commissioner and shall comply with professionally accepted mass appraisal techniques."[84]

The Tax Commissioner has been delegated the authority to promulgate rules and regulations to set standards for the appraisal of real property by county assessors.[85] These rules and

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[79] *Omaha Country Club v. Douglas County Board of Equalization*, 11 Neb.App. 171, 645 N.W.2d 822, 825 (2002) (citations omitted).
[80] *Omaha Country Club v. Douglas County Board of Equalization*, 11 Neb.App. 171, 645 N.W.2d 822, 829 (2002) (citing 350 Neb. Admin. Code, ch. 10 §001.01 (2000) and 350 Neb. Admin. Code, ch. 10 §01.01F (2000)).
[81] *Omaha Country Club v. Douglas County Board of Equalization*, 11 Neb.App. 171, 645 N.W.2d 822, 831 (2002).
[82] See, 350 Neb. Admin. Code, ch. 10 §001.01 (2000) and 350 Neb. Admin. Code, ch. 10 §001.01 (03/2009); See also, 350 Neb. Admin. Code, ch. 10 §01.01F (2000) and 350 Neb. Admin. Code, ch. 10 §01.01F (03/2009).
[83] See, Neb. Rev. Stat. §77-1333 (Reissue 2009); See also, Nebraska Laws 2005, LB 263, §6 and Nebraska Laws 2007, LB334, §68.
[84] Neb. Rev. Stat. §77-1333(1) (Reissue 2009).
[85] See, Neb. Rev. Stat. §77-1301.01 (Reissue 2009).

regulations must be consistent with Nebraska Statutes sections 77-112 through 77-201.[86] Following the *Omaha Country Club* decision, the Tax Commissioner produced rules and regulations concerning the assessment of LIHTC properties using the income approach.[87] Rules and regulations that are properly adopted and filed with the Secretary of State have the force and effect of statutory law.[88]

While the statutes and rules and regulations examined by the Nebraska Court of Appeals in *Omaha Country Club* are substantially similar, a factual difference exists concerning the lessees of the Subject Property and the Nebraska Investment Finance Authority (NIFA),[89] the entity owning a partial interest in the Subject Property. In *Omaha Country Club* the lessee was not an exempt entity. NIFA is "not a state agency, but an independent instrumentality exercising essential public functions[.]"[90] Article VIII, section 2 of the Nebraska Constitution exempts from taxation property of the state or its political subdivisions. The Legislature has specifically declared that all property acquired by NIFA in the furtherance of its delegated purposes "is declared to be public property."[91] The Legislature clarified that "[t]he property to the extent such property is used for a public purpose… shall at all times be exempt from all taxes[.]"[92] It is clear that the Legislature has defined property owned by NIFA in the furtherance of its duties as property of the state, and that property is clearly exempted from taxation by Article VIII, section 2 of the Nebraska Constitution.

Federal law requires each state to designate a housing credit agency for the purpose of allocating low-income housing tax credits, to administer the low-income housing tax credit program, and to monitor low-income housing tax credit developments for noncompliance.[93] Nebraska has designated NIFA as the applicable housing credit agency. The legislative purpose of the development of NIFA includes to, "[e]ncourage the investment of private capital and stimulate the construction of sanitary, safe, and uncrowded housing for low-income and

[86] See, *id*.
[87] See, 350 Neb. Admin. Code, ch. 51 (03/15/2009).
[88] See, *Smalley v. Nebraska Department of Health and Human Services*, 283 Neb. 544, 557, 811 N.W.2d 246, 256 (2012) (Citations Omitted).
[89] See, Neb. Rev. Stat. §58-226 (Reissue 2009).
[90] See, Neb. Rev. Stat. §58-226 (Reissue 2009).
[91] Neb. Rev. Stat. §58-268 (Reissue 2009).
[92] *Id*.
[93] See generally, 26 U.S.C. §42.

moderate-income person[.]"[94] NIFA was created, in part, to alleviate an inadequate supply of acceptable low-income housing.[95] The Legislature has declared that encouraging private investment in order to alleviate this problem is a "public purpose[.]"[96] Thus, the present appeal is distinguished from the case in *Omaha Country Club*.

In *Omaha Country Club*, all real property interests and estates were owned by taxable entities.[97] However, in the present appeal, Ederer is correct that the development of the income approach, as required by the rules and regulations promulgated by the Tax Commissioner, does not result in a determination of the fee simple interest. However, this is not contrary to Nebraska law. Instead, the regulatory scheme merely acknowledges what is constitutionally and statutorily required; that the property interest held by NIFA during the term of the LURA is exempt from taxation.[98] The Commission only has jurisdiction over the Taxpayer and over the determination of the actual value of the Subject Property owned by the Taxpayer. The Taxpayer, not NIFA, is responsible for the taxes associated with the actual value of that portion of the Subject Property owned by the Taxpayer. Indeed, outside of the limited statutory framework regarding leased public property for a non-public purpose, a lessee never incurs a tax liability under Nebraska Statute for leased property, although it may elect to pay taxes as part of a lease.[99]

The Commission finds that the assessment of rent-restricted property according to the rules and regulations found in 350 Neb. Admin. Code, ch. 51 (03/15/2009) does not violate the requirement that real property, other than agricultural land and horticultural land, should be assessed at its actual value. The Commission finds that the County Board's determinations which relied upon Ederer's assessments do not comport with the Tax Commissioner's properly promulgated rules and regulations and are unreasonable or arbitrary.

[94] See, Neb. Rev. Stat. §58-203(1)(a) (Reissue 2009).
[95] See, Neb. Rev. Stat. §58-202(2)(c) (Reissue 2009).
[96] Neb. Rev. Stat. §58-203(2) (Reissue 2009).
[97] *Omaha Country Club v. Douglas County Board of Equalization*, 11 Neb.App. 171, 645 N.W.2d 822, 824 (2002).
[98] However, no part of this order should be construed as determining NIFA's tax liability of any portion of the Subject Property.
[99] See, Neb. Rev. Stat. §77-202.11 (Reissue 2009).

3. Actual Value of the Subject Property

A. Net Operating Income

Weinberg conducted two appraisals of the Subject Property for tax years 2012 and 2013, and one for tax year 2014.[100] He expressed opinions of value of $1,750,000 and $1,690,000 for tax year 2012.[101] He expressed opinions of value of $1,790,000 and $1,770,000 for tax year 2013.[102] His opinion of value for tax year 2014 was $1,670,000. The Taxpayer asserted that the later appraisal contained in Exhibit 24 was the most accurate and was the appraisal upon which Weinberg based his opinions of value at the hearing.

Weinberg's NOI calculations contain three important errors: (1) Weinberg failed to include the income associated with the unit occupied by onsite management;[103] (2) Weinberg applied the vacancy and collection loss rate to Other Income;[104] and (3) Weinberg included the property taxes as an expense.[105]

First, one unit was occupied by the resident manager as permitted by the LURA.[106] The Taxpayer made a managerial decision to provide the resident manager a rent-free apartment onsite as an employment benefit.[107] This is not required by the LURA, but is a managerial decision. The Taxpayer could choose to charge the resident manager rent and supply adequate compensation some other way, or could choose to lease out the unit to a qualified tenant. The assessment of real property is intended to derive the actual value of real property and not the particular value to the owner based upon managerial decisions.[108] The Commission finds that the NOI should include the rental income for the unit that was occupied by the resident manager.

Second, the vacancy and collection loss rate is only applicable to income derived from the Subject Property which is affected by a reduction in the occupancy, tenant turnover, and the

[100] See, E20:134-251 and E24.
[101] See, E20:218 and E24:85.
[102] See, E20:218 and E24:85.
[103] See, E24:71
[104] See, E24:71.
[105] See, E24:71.
[106] See, E20:19.
[107] See, E24:71.
[108] See, International Associations of Assessing Officers, *Fundamentals of Mass Appraisal*, at 172-74 (2011) (indicating that the income factors should be derived from what is typical in the market and not include the effects of management decisions).

failure of tenants to pay rent.[109] The effective gross income (EGI) is calculated by subtracting the vacancy and collection loss from the potential gross income (PGI) and then adding the miscellaneous income into the remainder.[110] The other income in Weinberg's calculation of the PGI included "interest from income, late charges, [and] special service fees[.]"[111] The vacancy and collection loss should not be applied to these miscellaneous expenses.[112]

With this correction, Weinberg's recalculated EGI of $345,926.00 for tax year 2012 is as follows:[113]

2012

Units	**Rent**	**Monthly**	**Months**	**Annual**	
16	$548.00	$8,768.00	12	$105,216.00	
8	$615.00	$4,920.00	12	$59,040.00	
15	$660.00	$9,900.00	12	$118,800.00	
8	$741.00	$5,928.00	12	$71,136.00	
1 (Manager's Unit)	$660.00	$660.00	12	$7,920.00	
48	$3,224.00	$30,176.00		**$362,112.00**	**PGI**
				$18,106	**V&C Loss**
			Total	$344,006	
		Units	Income		
		48	$40	$1,920.00	
				$345,926	**EGI**

109 See, The Appraisal Institute, *The Appraisal of Real Estate,* at 478-79 (14th ed. 2013).
110 See, International Association of Assessing Officers, *Property Assessment Valuation,* at 325-26 (3rd ed. 2010).
111 See, E20:197.
112 See, International Association of Assessing Officers, *Property Assessment Valuation,* at 325-26 (3rd ed. 2010).
113 See, E24:71 (indicate maximum rents by unit and other income).

With the same correction, Weinberg's recalculated EGI of $352,128.00 for tax year 2013 is as follows:[114]

2013

Units	Rent	Monthly	Months	Annual	
16	$558.00	$8,928.00	12	$107,136.00	
8	$626.00	$5,008.00	12	$60,096.00	
15	$672.00	$10,080.00	12	$120,960.00	
8	$754.00	$6,032.00	12	$72,384.00	
1 (Manager's Unit)	$672.00	$672.00	12	$8,064.00	
48	$3,282.00	$30,720.00		**$368,640.00**	**PGI**
				$18,432.00	**V&C Loss**
			Total	$350,208.00	
		Units	Income		
		48	$40	$1,920.00	
				$352,128.00	**EGI**

And with the same correction, Weinberg's recalculated EGI of $347,568.00 for tax year 2014 is as follows:[115]

2014

Units	Rent	Monthly	Months	Annual	
16	$549.00	$8,784.00	12	$105,408.00	
8	$618.00	$4,944.00	12	$59,328.00	
15	$664.00	$9,960.00	12	$119,520.00	
8	$746.00	$5,968.00	12	$71,616.00	
1 (Manager's Unit)	$664.00	$664.00	12	$7,968.00	
48	$3,241.00	$30,320.00		**$363,840.00**	**PGI**
V&C @5%	0.05			**$18,192.00**	**V&C Loss**
			Total	$345,648.00	
		Units	Income		
Other Income		48	$40	$1,920.00	
				$347,568.00	**EGI**

[114] See, E24:71 (indicate maximum rents by unit and other income).
[115] See, E24:71 (indicate maximum rents by unit and other income).

Finally, when determining the assessed value of real property, the property taxes should be included in the capitalization rate instead of in the expenses.[116] Ad valorem taxes are, by nature, dependent upon the assessed value of real property. It is circular to determine the amount of property taxes to be paid as an expense when the appraisal has yet to derive the assessed value of the real property. Therefore, the Commission accepts Weinberg's expense calculations, as adjusted to remove the property taxes, as follows:[117]

Expenses 2012		
	Ad. & Mark	$28,800.00
	Main.	$21,600.00
	Payroll	$49,800.00
	Utilities	$33,600.00
	Insurance	$9,600.00
	Rep. Reserves	$14,400.00
	Management	$20,298.00
	Payroll +	$7,920.00
	Total	**$186,018.00**

Expenses 2013		
	Ad. & Mark	$29,520.00
	Main.	$22,140.00
	Payroll	$51,045.00
	Utilities	$34,440.00
	Insurance	$9,840.00
	Rep. Reserves	$14,760.00
	Management	$20,662.00
	Payroll +	$8,064.00
	Total	**$190,471.00**

[116] See, International Association of Assessing Officers, *Property Assessment Valuation*, at 332 (3rd ed. 2010).
[117] See, E24:71 (indicating the expenses by tax year).

Expenses 2014		
	Ad. & Mark	$30,258.00
	Main.	$22,694.00
	Payroll	$52,321.00
	Utilities	$35,301.00
	Insurance	$10,086.00
	Rep. Reserves	$14,760.00
	Management	$20,394.00
	Payroll +	$7,968.00
	Total	**$193,782.00**

After the necessary adjustments, the Commission determines that the NOI is $159,908 for tax year 2012,[118] $161,657 for tax year 2013,[119] and $153,786 for tax year 2014.[120]

B. Capitalization Rate

In his later appraisal, Weinberg calculated his capitalization rate based upon a market extraction method using sales of unrestricted apartment complexes.[121] Based upon its reasoning stated above, the Commission finds that the use of sales of unrestricted apartment complexes to determine the actual value of the Subject Property inappropriately ignores the decreased risks associated with ownership of an LIHTC property. Weinberg's previous appraisal found in evidence at Exhibit 20 calculated the Subject Property's capitalization rate using the debt coverage ratio technique (DCR) and the band of investment method.[122] However, Weinberg performed these methods using data obtained from unrestricted rental properties.[123] Weinberg asserted it was reasonable not to take the tax credits into account when determining the capitalization rate because his experience indicated that considering the tax credits ultimately resulted in higher capitalization rates when using the discounted cash flow analysis. Weinberg asserted that it is contrary to logic that restricted properties would be a riskier venture than a market property. The Commission agrees that it is unreasonable that LIHTC properties would have a higher capitalization rate than market rent properties, but as indicated below, the

[118] $345,926 EGI – $186.018 expenses = $159,908 NOI.
[119] $352,128 EGI – $190,471 expenses = $161,657 NOI.
[120] $347,568 EGI – $193,782 expenses = $153,786 NOI.
[121] See, E23:24:67-70.
[122] See, E20:207.
[123] See, E20:202.

Commission disagrees that any analysis which includes the tax credits would necessarily result in a higher capitalization rate.

Generally, tax incentives intended to produce a specific type of economic activity only work when the incentive is sufficient to create a greater financial return from the incentivized economic activity than from other alternate economic activities. Here the return on investment for limited partners is the access to tax credits. In order for the LIHTC program to function, the return on investment for tax credits would need to exceed the return on investment for other economic activities, either through a monetarily higher return or a less risky investment. In this appeal, the increased risk associated with the restricted rent and limited income is erased and exceeded by security gained from the limited partners' investment in the equity of the project in return for access to the ownership privilege of tax credits. Moreover, the partners benefit from the ability to write off depreciation and loss from the project on subsequent income tax calculations due to pass through provisions in the Taxpayer's founding documents.[124]

This principle is illustrated when the debt coverage ratio method and the band of investment method take into account the Subject Property's true debt to equity ratio. The derived capitalization rates indicate a lower risk for rent restricted properties. The testimony in the hearing indicated that the Subject Property's financing was typical for LIHTC properties. Additionally, the NOI is calculated based, to the extent possible, on market expenses and income. The capitalization rate applied to the Subject Property should be derived from the market in order to avoid valuing the management of the Subject Property. Because all indications are that the Subject Property is typical, where specific market factors are unknown, the Subject Property's actual factors can be substituted and still derive a reasonable capitalization rate. The NOI from each year can be analyzed assuming each was the first year of the project to provide a range of potentially applicable capitalization rates.

C. Debt Coverage Ratio

The Debt Coverage Ratio (DCR) is "the ratio of net operating income to annual debt service (I_M), of the payment that covers interest on and retirement of the outstanding principal of the

[124] See, E20:111-112.

mortgage loan: DCR = I_0/I_M[.]"[125] In the DCR formula, I_0 equals the net operating income for the Subject Property, and (I_M) equals the debt service associated with the mortgages secured against the Subject Property.[126] Once the DCR is calculated, it is multiplied by the mortgage capitalization rate (R_M) and the loan-to-value ratio (M) to derive the overall capitalization rate; mathematically expressed as R_O = DCR x R_M x M.[127] R_M equals the annual debt service divided by the mortgage principal.[128] M equals "the ratio between a mortgage loan and the value of the property pledged as security, usually expressed as a percentage."[129] Debt service is, "[t]he periodic payment, expressed on an annual basis, that covers the interest on, and for an amortizing loan the retirement of, the outstanding principal of a mortgage loan…"[130] The debt service calculation is expressed mathematically as monthly debt service = P I(1 + I)^n /(1 + I)^n – 1 where monthly debt service equals the monthly payment, P equals the principal, I equals the interest rate, and n the term of the loan expressed in months. Monthly debt service is then multiplied by 12 to derive the annual debt service.

The typical LIHTC property is financed by 20% debt and 80% equity investment. The annual debt service is then dependent upon the debt with a principal of 20% of the cost of the Subject Property. The Taxpayer's financial statement included in evidence indicates an equity investment of $6,178,218 for the construction of the Subject Property, excluding the cost of furniture, fixtures, and equipment (FF&E).[131] The debt associated with the construction of the Subject Property, based on the typical debt to equity ratio for an LIHTC property, is therefore $1,235,644.[132]

The annual debt service for the Subject Property is based on a typical 20% debt ratio deriving a principal of $1,235,644. The Taxpayer asserted that the mortgages held against the Subject Property were typical for restricted properties. The Commission therefore applies the terms of the Subject Property's mortgage at 6.25% interest over 15 years.[133] The annual debt service is

[125] The Appraisal Institute, *The Appraisal of Real Estate,* at 498 (14th ed. 2013).
[126] See, *id*.
[127] See, *id*.
[128] See, *id*. at 496.
[129] *Id*.
[130] See, *id*. at 498.
[131] See, E20:117.
[132] $6,178,218 x.2 = $1,235,644.
[133] See, E20:118.

$127,136.[134] As previously discussed, the NOI of the Subject Property has been calculated for all three years. The DCR is therefore 1.257771 for tax year 2012,[135] 1.271528 for tax year 2013,[136] and 1.209618 for tax year 2014.[137]

The R_M factor is also easily calculable because the annual debt service and principal are known. The applicable R_M factor is .10289.[138]

M is supplied by the typical debt to equity ratio. M equals "the ratio between a mortgage loan and the value of the property pledged as security, usually expressed as a percentage."[139] To calculate the ratio of the principal to the value of the Subject Property pledged as security the Commission again applies the typical debt to equity ratio of 20%:80%. M is therefore equal to 20% or .2.

The rounded unloaded overall capitalization rates as derived from the DCR method are, therefore, 2.6% for tax year 2012,[140] 2.6% for tax year 2013,[141] and 2.5% for tax year 2014.[142]

D. Band of Investment Method

The band of investment method calculates the overall capitalization rate by considering the capitalization rates for the debt and equity and combining them to derive an overall capitalization rate for the Subject Property. The applicable equation is:

$R_O = (M \times R_M) + ((1-M) \times R_E)$.

Similar to the Debt Coverage Ratio method R_O equals the unloaded overall capitalization rate, M equals "the ratio between a mortgage loan and the value of the property pledged as security, usually expressed as a percentage[,]" and R_M equals the annual debt service divided by the mortgage principal.[143] The calculations of these factors from the previous section are

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134 ($1,235,644)(.0625/12)((1+(.0625/12))^180/(1+(.0625/12))^180 – 1)) = $10,594.67 x 12 = $127,136.
135 $159,908/$127,136 = 1.257771.
136 $161,657/$127,136 = 1.271528.
137 $153,786/$127,136 = 1.209618.
138 $127,136/$1,235,644 = 1.0289.
139 *Id*.
140 1.257771 DCR x .10289 R_M x 0.2 M = .0258825 R_O.
141 1.271528 DCR x .10289 R_M x 0.2 M = .0261656 R_O.
142 1.209618 DCR x .10289 R_M x 0.2 M = .0248916 R_O.
143 The Appraisal Institute, *The Appraisal of Real Estate*, at 496-498 (14th ed. 2013).

applicable in the band of investment method as well. Additionally, the R_E, or equity capitalization rate, is necessary to derive the capitalization rate.[144]

R_E is derived by dividing the pre-tax cash flow by the equity invested.[145] The Commission notes that Weinberg testified concerning the limited partners equity yield rate (Y_E). The Commission notes that Y_E and R_E are not the same thing. R_E, the equity capitalization rate, seeks to express the risks associated with the equity investment in the real property.[146] On the other hand, Y_E, the equity yield rate, is the "rate of return on equity capital as distinguished from the rate of return on debt capital; the equity investor's internal rate of return. The equity yield rate considers the effect of debt financing on the cash flow to the equity investor."[147] The rate of return on equity capital, Y_E, may be more or less than R_E,[148] "[a]n income rate that reflects the relationship between a single year's pre-tax cash flow and the equity investment."[149] The band of investment requires the use of R_E, which again is derived by dividing the pre-tax cash flow by the equity invested.[150]

The pre-tax cash flow is derived by taking the NOI and subtracting the annual debt service and the cost of capital improvements, and adding any interest gained or loan proceeds acquired. The NOI and annual debt service for the Subject Property are known, and there is no indication of any interest gained or loan proceeds acquired. The pre-tax cash flow is then easily derived by subtracting the annual debt service from the NOI. The pre-cash flow is $32,772 for 2012,[151] $34,521 for 2013,[152] and $26,650 for 2014.[153]

The equity investment is derived from the amount of money invested into the Subject Property.[154] The equity investment should not be confused with the equity of the property. The equity of the property denotes the value of an owner's interest in a property after all liens and

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[144] See, *id*. at 496.
[145] See, *id*.
[146] See, *id*.
[147] Appraisal Institute, *The Dictionary of Real Estate Appraisal*, at 100 (4th ed. 2002) (definition of equity yield rate).
[148] See, The Appraisal Institute, *The Appraisal of Real Estate*, at 496 (14th ed. 2013)(indicating that Y_E and R_E are not the same thing and may not be equal to one another).
[149] Appraisal Institute, *The Dictionary of Real Estate Appraisal*, at 99 (4th ed. 2002) (definition of equity capitalization rate).
[150] See, *id*.
[151] $159,908 NOI - $127,136= $32,772 pre-tax cash flow.
[152] $161,657 NOI - $127,136= $34,521 pre-tax cash flow.
[153] $153,786 NOI - $127,136= $26,650 pre-tax cash flow.
[154] See, Appraisal Institute, *The Dictionary of Real Estate Appraisal*, at 98 (4th ed. 2002) (defining equity is part as "ownership claim on property"); See also, Appraisal Institute, *The Dictionary of Real Estate Appraisal*, at 151 (4th ed. 2002) (defining investment in part as "monies placed in a property for long term use, usually with the expectation of profit").

claims,[155] whereas the equity investment indicates the amount of money invested in the property.[156] Again, the financial statement indicates a total cost of $6,178,218 for the Subject Property, and applying the 20:80 debt to equity ratio, this would indicate an equity investment of $4,942,574.

Having calculated the pre-tax cash flow and equity investment, R_E is .006631 for tax year 2012,[157] .006984 for tax year 2013,[158] and .005392 for tax year 2014.[159]

With all factors known, the band of investment method can be utilized for all three tax years and derives rounded unloaded overall capitalization rates of 2.6% for tax year 2012,[160] 2.6% for tax year 2013,[161] and 2.5% for tax year 2014.[162]

E. Conclusion

The preceding calculations indicate an unloaded overall capitalization rate for the Subject Property between 2.5% and 2.6%. In fact, based upon the known information, the band of investment method and DCR method produced identical capitalization rates from the NOIs within the same tax year. The capitalization rate can be loaded with the effective tax rate. The derived effective tax rate is 2.2%.[163] The indicated loaded capitalization rate for the Subject Property is, therefore, 4.7% to 4.8%. The Commission determines that the applicable loaded capitalization rate for all years at issue is 4.75%.

F. Calculation of the Actual Value of the Subject Property

With the known components of the income approach the actual value of the Subject Property for tax years 2012, 2013, and 2014 can be calculated. The calculated actual value of the Subject Property for tax year 2012 is $3,366,484.[164] The calculated actual value of the Subject Property

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155 See, Appraisal Institute, *The Dictionary of Real Estate Appraisal*, at 98 (4th ed. 2002) (second definition of equity).
156 See, Appraisal Institute, *The Dictionary of Real Estate Appraisal*, at 98 (4th ed. 2002) (second definition of equity); See also, Appraisal Institute, *The Dictionary of Real Estate Appraisal*, at 151 (4th ed. 2002) (second definition of investment).
157 R_E = $32,772 pre-tax cash flow/$4,942,574 Equity Investment = .006631.
158 R_E = $34,521 pre-tax cash flow/$4,942,574 Equity Investment = .006984.
159 R_E = $26,650 pre-tax cash flow/$4,942,574 Equity Investment = .005392.
160 $(.2\ M)(\ .10289\ R_M) + ((1-.2\ M)(.006631\ R_E) = .025883$.
161 $(.2\ M)(\ .10289\ R_M) + ((1-.2\ M)(.006984\ R_E) = .026166$.
162 $(.2\ M)(\ .10289\ R_M) + ((1-.2\ M)(.005392\ R_E) = .024892$.
163 See, E4:1, E5:1, and E6:1.
164 $159,908 NOI / .0475 = $3,366,484.

for tax year 2013 is $3,403,305.[165] The calculated actual value of the Subject Property for tax year 2014 is $3,237,600.[166]

The Commission finds that there is clear and convincing evidence that the County Board's determinations of the taxable values of the Subject Property were arbitrary or unreasonable. However, the Commission may not order an increase in taxable value for a given year from the highest taxable value for which notice was given to the Taxpayer for that year.[167] In the present case, there is no evidence that the Taxpayer was given notice of any taxable value higher than $2,030,000 for tax year 2012,[168] $2,530,000 for tax year 2013,[169] and $2,530,000 for tax year 2014.[170]

The Commission's Rules and Regulations do not allow the Commission to set taxable value of real property at any amount higher than previously noticed to the Taxpayer by the County Assessor, the County Board, or the Property Tax Administrator without specific notice from the opposing party prior to the hearing that the opposing party intends to offer evidence and assert that the taxable value for the Subject Property is higher than any previously noticed value.[171] The Commission notes that the County Board did not assert during the hearing that the taxable value should be increased above that value previously noticed, and that no notice as would be required by the Commission's Rules and Regulations was ever perfected. Therefore, the Commission finds that it cannot set the taxable value of the Subject Property at any amount higher than previously noticed to the Taxpayer by the County Assessor, County Board, or Property Tax Administrator. Based upon the foregoing, the Commission finds that the County Board's determinations should not be reversed because of the valuation errors.

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 determinations. The Commission also finds that there is clear and convincing evidence that the

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165 $161,657 NOI / .0475 = $3,403,305.
166 $153,786 NOI / .0475 = $3,237,600.
167 Title 442 Neb. Admin. Code, ch 5, §016.02A (06/06/11).
168 See, E1.
169 See, E2.
170 See, E3.
171 Title 442 Neb. Admin. Code, ch 5, §016.02A (06/06/11).

County Board's decisions were arbitrary or unreasonable. However, for the reasons set forth above, the determinations of the County Board should be affirmed.

VI. ORDER

IT IS ORDERED THAT:

1. The decisions of the Sarpy County Board of Equalization determining the taxable values of the Subject Property for tax years 2012, 2013 and 2014 are affirmed.[172]
2. The taxable value of the Subject Property for tax year 2012 is $2,030,000.
3. The taxable value of the Subject Property for tax year 2013 is $2,530,000.
4. The taxable value of the Subject Property for tax year 2014 is $2,530,000.
5. This Decision and Order, if no appeal is timely filed, shall be certified to the Sarpy County Treasurer and the Sarpy County Assessor, pursuant to Neb. Rev. Stat. §77-5018 (2014 Cum. Supp.).
6. Any request for relief, by any party, which is not specifically provided for by this Decision and Order is denied.
7. Each party is to bear its own costs in this proceeding.
8. This Decision and Order shall only be applicable to tax years 2012, 2013, and 2014.
9. This Decision and Order is effective for purposes of appeal on June 17, 2015.[173]

Signed and Sealed: June 17, 2015

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Robert W. Hotz, Commissioner

SEAL

____
Nancy J. Salmon, Commissioner

[172] Taxable 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.
[173] Appeals from any decision of the Commission must satisfy the requirements of Neb. Rev. Stat. §77-5019 (2014 Cum. Supp.) and other provisions of Nebraska Statutes and Court Rules.