BEFORE THE STATE TAX APPEAL BOARD

OF THE STATE OF MONTANA

CONTINENTAL DEVELOPMENT, INC, Appellant,	)	DOCKET NO.: PT-2002-18
-vs-	)	
THE DEPARTMENT OF REVENUE OF THE STATE OF MONTANA, Respondent.	)	FACTUAL BACKGROUND, CONCLUSIONS OF LAW, ORDER and OPPORTUNITY FOR JUDICIAL REVIEW

The above-entitled appeal was heard on January 13, 2004, in the City of Helena, in accordance with an order of the State Tax Appeal Board of the State of Montana (the Board). The notice of the hearing was duly given as required by law.

Robert Sterup, Attorney, represented Continental Development, Inc. Jim Colla, partner/stockholder and Cheryl A. Cordeiro, V.P., presented testimony in support of the appeal. Mark Prichard, Attorney, represented the Montana Department of Revenue (DOR). Jim Fairbanks, Appraiser/Region Four Manager, testified in support of the respondent. In addition to testimony, exhibits were received in evidence. The record remained open affording the parties an opportunity to supplement the record with additional exhibits at the request of the Board. The parties also requested that they be given the opportunity to brief the supplemental exhibits.

The Taxpayer is the appellant in this proceeding and, therefore, has the burden of proof. In addition, the DOR has a burden of proof in supporting its market value determination. (Western Airlines, Inc., v. Catherine Michunovich et al., 149 Mont. 347, 428 P.2d 3, (1967).

Based on the evidence and testimony, this Board finds that the DOR properly classified and valued the property as individual condominium units. The market value of the individual condominium units is modified as outlined in the following opinion.

STATEMENT OF THE ISSUE

The issues before this Board are (1) the classification of the property as a commercial apartment complex versus single-family residential condominium units, and, (2) the market value pursuant to MCA §15-8-111.

FACTUAL BACKGROUND

1. Due, proper and sufficient notice was given of this matter, the hearing hereon, and of the time and place of the hearing. All parties were afforded the opportunity to present evidence, oral and documentary.

2. The subject property is described as the Cottonwoods at Grant Creek, with a legal description of:

> Parcel 3 of Certificate of Survey No. 5125, located in the NW1/4 of Section 5, Township 13 North, Range 19 West, P.M.M., Missoula County, Montana, Less

that portion conveyed to the City of Missoula, and improvements located thereon. DOR Exhibit B identifies the individual units by address and Geo-Code unit #.

3. The DOR testified that each condominium unit is being assessed for a portion of the total land value. Each unit's portion of land value amounts to $15,000. This would suggest a total land value of $1,530,000 ($15,000 X 102).

4. The Taxpayer purchased the property in August of 2001 for $6,100,000 (Appellant Exhibit #1).

5. At the time the Taxpayer purchased the property it was being operated solely as an apartment complex consisting of:

- Seventeen (17) residential buildings containing a total of one hundred two (102) apartment units:
  - Eight (8) 1-bedroom/1-bathroom units.
  - Eighty-six (86) 2-bedroom/2-bathroom units.
  - Eight (8) 3-bedroom/2-bathroom units.
- Three (3) garage buildings containing a total of twenty-four (24) garage/storage units.
- One hundred ninety-one (191) parking spaces:
  - Eighty-seven (87 open parking spaces.
  - One hundred four (104) covered parking spaces (carports).

6. Continental Development, Inc., purchased the Cottonwoods under the guidelines of the IRC Section 1031 tax-deferred exchange.

7. First Interstate Bank ordered an independent fee appraisal for mortgage purposes on the Cottonwoods. The appraisal suggests an indication of value at five million six hundred thousand

dollars ($5,600,000), and an effective date of value of July 11, 2001 (Joint Exhibit #1).

8. Continental Development, Inc., filed the “Declaration of Condominiums” document with Missoula County, which is dated October 15, 2001 (Joint Exhibit #2).

9. For tax year 2000, 2001 and 2002 the DOR’s appraised values for the subject are:

Year	Value
2000	$4,736,000 (Appellant Exhibit 8)
2001	$4,608,600[1] (Appellant Exhibit 9)
2002	$$7,937,700[2] (DOR Exhibit B)

10. For tax year 2002 the DOR sent the Taxpayer an individual assessment notice for each condo unit and one for the 24 garages.

11. On June 17, 2002, the Taxpayer filed the AB-26 form, requesting an informal review, stating:

> This property was purchased by the taxpayer on 8/27/2001 for $6,100,000. The current tax appraisal totals approximately $7,936,000, which is greatly in excess of market value as shown by the purchase price.

12. On October 16, 2002, the DOR denied any reduction in value stating:

> As a result of this informal review, an adjustment was not made for the following reasons: Absence of persuasive documentation in support of alternate values.

13. On September 14, 2002, the Taxpayer appealed the DOR’s AB-26 decision to the Missoula County Tax Appeal Board (MCTAB) stating:

> This property was purchased by the taxpayer 8/27/01 for $6,100,000. The current tax appraisal is greatly in excess of market value as shown by the purchase price.

14. On December 17, 2002, the MCTAB denied the Taxpayer's appeal stating:

> The units have been converted from apartments to condominiums. Thereby increasing the sales value of each individual unit.

15. On January 10, 2003, the Taxpayer appealed the MCTAB decision to this Board stating:

> Units are still rented as apartments – No improvements were made to the property – Appraised value was only $5,600,000 – filing condo declaration should not increase taxes.

16. The Board established a post-hearing scheduling order for the parties to submit additional evidence and testimony. In addition, the Board requested that additional questions be answered per an order dated April 1, 2004.

TAXPAYER'S CONTENTIONS

Mr. Colla testified that the subject was purchased for $6,100,000, but appraised for mortgage purposes at $5,600,000. The purchase involved the IRC Section 1031 Tax Deferred Exchange. He testified, *"…You may end up paying a little more than you normally would for it because there's a tax consequences…"*

Mr. Colla indicated that the bank would only loan $4,100,000 on the property, so additional money was required from the buyer in order for the loan to close. He indicated he

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1 Value reduction due to land area reduction.

personally loaned the corporation an additional $800,000. Mr. Colla testified that the bank was not opposed to the conversion to condominiums, but the loan would be made based upon the properties use as rental units or an apartment complex. In addition, when an individual unit sold, the bank would receive two-thirds of the purchase price towards the balance of the loan. Mr. Colla also testified that there would be adverse tax implications, under IRC Section 1031, if the condominium units were sold off in a short term. The intent was not to sell all the units, but rather retain a portion solely for the use of rental apartments for the generation of income.

Mr. Colla indicated that, when an individual unit is sold, the tax burden is then shifted to the new owner. He testified, *"…it's a pretty good deal for the State at that point, because once we sell them you are going to come in and reappraise it, and I assume appraise it at the rate that we sold it at, and all of the sudden the tax base in that area starts going up…"*

Mr. Colla suggests it's rather absurd that the property sold for $6,100,000, appraised for $5,600,000, and four months later is valued by the State of Montana for $7,937,700, when nothing physically has changed with the property. At the time of the sale, all 102 units were still being used as rental

2 Value for 102 condominium units and 24 garage units.

apartments. There is no reason that the value should have been revised because the property was converted into condominiums.

Through questioning of commercial property versus residential/single-family property, it is the opinion of Mr. Colla that the units that are owned by Continental and are operated as rental property are more in line with a commercial designation, because of the income potential. The units that have been sold and occupied by the buyer are residential property or a single-family dwelling. The property or units should be valued based upon the income being generated and, once the property is sold as a single-family dwelling, it then has a new value.

Mr. Colla testified that, as some of the units are sold and the note is paid, the remaining rental units retained by Continental, at some point, would begin to cash flow.

Ms. Cordeiro offered testimony in support of the appeal. She is responsible for accounting/bookkeeping, overseeing the management company, and dealing with the real estate agent(s) when a unit is sold.

Ms. Cordeiro testified that upon the advice of an accountant, Continental would be limited as to the number of units that could be sold because of limitations associated with the IRC Section 1031 Tax Deferred Exchange. For a period of two years Continental should not aggressively sell many units because of the appearance of the condominiums being held as inventory.

Ms. Cordeiro testified that a representative for Continental had discussions with Jim Fairbanks, with regards to the tax implications associated with the conversion from apartments to condominiums. It was reported to her that from those discussions, the real estate taxes would only increase slightly, possibly 5% to 10%.

Ms. Cordeiro testified that she met with Mr. Fairbanks after the DOR reappraised the property to discuss Continentals business plan. *"…Certainly we didn't have a problem if we sold a unit and they wanted to assess at that new appraised value, or assessed value, but certainly we are keeping them as apartments and that was just a terrible burden for us, just did not seem fair"*. Ms. Cordeiro testified that when the sale of a unit is completed, the new owner assumes the tax burden.

Ms. Cordeiro testified that the sales prices for the units as listed on Joint Exhibit #3 varied depending on the unit size, inclusion of a garage, and unit amenities, i.e. location, view, etc. She also indicated that had Continental listed all 102 units for sale at one time, it is very doubtful those sales prices would have been attained.

It is also the opinion of Ms. Cordeiro that the filing of the condominium documents should not result in an increased value when the units are being rented.

Ms. Cordeiro testified that there is no incentive to convert an apartment complex to condominiums if the value were to increase so substantially. Had Continental left the property as apartments, the value would have remained unchanged.

Ms. Cordeiro testified that the properties listed on Joint Exhibit #3 as “pending” have since closed. In addition, since Exhibit #3 was produced, six more units have sold.

Ms. Cordeiro testified that the original plan was to sell approximately one third of the units and retain ownership of the remaining units and operate them as rental property. Continental typically lists a unit for sale when it becomes vacant, if it falls within the business plan. The vacancy rate for the subject property has increased since the property was purchased which is a result of additional apartments being constructed in Missoula. Subsequent to increases in operating expenses, i.e., water rates, insurance, and real estate taxes, the number of units that Continental would retain in order to make the property cash flow needs to be reanalyzed.

Mr. Sterup questioned Mr. Fairbanks with respect to the DOR’s market value determination for tax years 2000, 2001, and

2002. The following table is a listing of the property values illustrated on Appellants Exhibit's 8, 9, and 10:

	Exhibit 8	Exhibit 9	Exhibit 10
Year	2000	2001	2002
Land Value	$492,600	$365,200	$1,530,000
Improvement Value	$4,243,400	$4,243,400	$6,407,700
Total Value	**$4,736,000**	**$4,608,600**	**$7,937,700**[3]

The reason the land value decreased from 2000 to 2001 was the result of a land split, reducing the total area owned by the Taxpayer.

Mr. Fairbanks testified that the DOR employed the sales comparison approach method in establishing the 2002 market value for all 102 units. He also testified that the DOR did not arrive at a value indication by means of an income approach.

Mr. Fairbanks agreed that the sales prices as listed on Joint Exhibit #3, may not have been achieved had Continental made the decision to list all 102 units for sale at one time.

Mr. Sterup asked the question of the DOR, *"Would it be possible to use the comparable sales model for condos, with respect to a specified percentage of the units, while using the apartment data, with respect to the other units"?* Mr. Fairbanks indicated that method would not work for valuing property within the DOR's Computer Assisted Mass Appraisal System (CAMAS).

3 Total value of all 102-condominium assessment notices.

DOR'S CONTENTIONS

Mr. Fairbanks testified that he was the DOR appraiser who established the market value for the Cottonwood Condominiums. Because the property is residential in nature, the method of appraisal utilized was the sales comparison approach. CAMAS selected comparable condominium sales when establishing the value for the 102 Cottonwood units. All 102 Cottonwood units were separately appraised and each received its own assessment notice pursuant to ***§15-8-511. Undivided interest in common elements of condominium project.*** *(1) Each unit of a condominium project is considered a parcel of real property subject to separate assessment and taxation* (emphasis added). Once the condominium document was filed, the DOR was bound by statute to appraise each unit separately.

Mr. Fairbanks testified that the CAMAS market modeling identified sales that occurred during 1994 through 1996. Based on Mr. Fairbanks testimony and Exhibit B, the DOR appraised the one, two, and three bedroom units, along with the twenty-four garages as follows:

	Baths	Unit Size (SF)	2002 Market Value	Total # Units	2002 Market Value
One Bedroom	1	701	$71,500	8	$572,000
Two Bedroom	2	928	$76,500	86	$6,579,000
Three Bedroom	2	1,168	$84,000	8	$672,000
Garages				24	$114,700
					$7,937,700

The DOR testified that, prior to the conversion to condominiums, the subject was identified as a commercial income-producing property. The DOR generated value indications by means of the cost approach along with the income approach. The DOR determined that the cost approach offered the best indication of value. When the property was converted, the DOR produced values from the cost approach along with the sales comparison approach, and relied upon the sales comparison approach as the final indication of value. And subsequent to the conversion, the property was classified as residential condominium.

Per the Board's request, the DOR supplemented the record with a value indication based upon a discounted cash flow (DCF) analysis or equity capitalization. The DOR's DCF reflects the following:

DISCOUNTED CASH FLOW ANALYSIS

Examination of rental income as units sell-out:

Rents during Sell-Out Period	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Rental TTL
NOI (Hogan report)	504,336	504,336	504,336	504,336	504,336	504,336	504,336	
Adjusted rents (+ 5% Yr)	504,336	529,584	556,064	583,867	613,060	643,713	675,899	
7 Year Absorption Rates	1.0000	0.8571	0.7143	0.5716	0.4287	0.2858	0.1429	
Annual NOI	504,336	453,907	397,196	333,738	262,819	183,973	96,586	
Discount Factor @ 9% (PW1)	0.917431	0.841680	0.772183	0.708425	0.649931	0.596267	0.547034	
Discounted Cash Flows	462,721	382,044	306,708	236,428	170,814	109,697	52,836	1,721,249

Examination of unit sales during sell-out:

Unit Sell-Out Period	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Sales TTL
2002 DOR appraisal	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	
7 Year Absorption Rates	0.1429	0.1429	0.1429	0.1429	0.1429	0.1429	0.1429	
Annual Sales	1,134,297	1,134,297	1,134,297	1,134,297	1,134,297	1,134,297	1,134,297	
Adjusted sales (+ 5% Yr)	1,134,297	1,191,012	1,250,563	1,313,091	1,378,745	1,447,683	1,520,067	
Sales expenses @ 6%	68,058	71,461	75,034	78,785	82,725	86,861	91,204	
Property taxes (less 2001 taxes in Hogan's report expenses)	58,456	50,103	41,755	33,413	25,060	16,707	8,353	
Net Sales	1,007,783	1,069,448	1,133,774	1,200,893	1,270,960	1,344,115	1,420,510	
Discount Factor @ 9% (PW1)	0.917431	0.841680	0.772183	0.708425	0.649931	0.596267	0.547034	
Discounted Cash Flows	924,572	900134	875,481	850,742	826,037	801,451	777,067	5,955,484
Cumulative Present Worth of Cash Flows:								**7,676,732**

BOARD'S DISCUSSION

When the Condominium document was filed and approved by the appropriate government officials, the legal description of the property was decisively modified. Rather than one property consisting of a 102-apartment complex, the property became 102 condominium units irrespective of the fact they were being used as rental property. Pursuant to ***§15-8-511. Undivided interest in common elements of condominium project.*** *(1) Each unit of a condominium project is considered a parcel of real property subject to separate assessment and taxation* (emphasis added). The DOR was correct when it appraised each property separately and mailed a separate assessment notice for each condominium unit.

The DOR is not without accountability; they must support the appraisal(s). If the conversion from apartments to condominiums was a value-altering event, then supporting market data must exist. *The Department of Revenue should, however, bear a certain burden of providing documented evidence to support its assessed values.* ***(Western Airlines, Inc., v. Catherine Michunovich et al., 149 Mont. 347, 428 P.2d 3,(1967).*** The DOR submitted as a post-hearing submission the market data or condominium sales that established values for the one, two, and three bedroom units. Summarized, these exhibits illustrate the following:

Comparable Sales – one bedroom units (Exhibit A)					
	Sale 1	Sale 2	Sale 3	Sale 4	Sale 5
Sale Date	9/2001	7/2001	9/1999	12/2000	9/2001
Sale Price	$85,000	$77,500	$82,000	$68,000	$117,000
Comparable Sales – two bedroom units (Exhibit B)					
	Sale 1	Sale 2	Sale 3	Sale 4	Sale 5
Sale Date	8/2000	5/2000	10/2001	10/2001	10/2000
Sale Price	$78,000	$78/000	$85,000	$85,000	$85,000
Comparable Sales – three bedroom units (Exhibit C)					
	Sale 1	Sale 2	Sale 3	Sale 4	Sale 5
Sale Date	6/2001	5/2001	10/2001	10/2001	8/2001
Sale Price	$112,500	$98,500	$94,500	$95,000	$94,000

§15-7-111. Periodic revaluation of certain taxable property.

(1) The department shall administer and supervise a program for the revaluation of all taxable property within classes three, four, and ten. All other property must be revalued annually. The revaluation of class three, four, and ten property is complete on December 31, 1996.

(3) Beginning January 1, 2001 the department of revenue shall administer and supervise a program for the revaluation of all taxable property within classes three, four, and ten. A comprehensive written reappraisal plan must be promulgated by the department. The reappraisal plan adopted must provide that all class three, four, and ten property in each county is revalued by January 1, 2003, and each succeeding 6 years (emphasis supplied).

This appeal was filed in 2002, the final year of the 1997 appraisal cycle. The market data that would be considered for that cycle would have occurred pre-1997. The market data that is illustrated on Exhibits A, B, and C, occurred from September 1999 through October 2001. Mr. Fairbanks testified, that when this property was converted to condominiums and revalued as such, the DOR was in the process of its most recent reappraisal, the 2003 cycle. Because new market data had been entered into the computer system, a “Comparable Sales” document could not be produced for the subject property. The sales price(s) that the Taxpayer is obtaining at the time this appeal was filed exceeds the DOR’s market value determinations. There have been no other sales data presented to consider. The sales prices the Taxpayer is currently obtaining may be considered by the DOR during the 2009 appraisal cycle.

The Taxpayer asserts that the legal change did not modify the value of the property because at the time the condominium document was filed, all the units were operated as rental property. If filing the condominium document as claimed by the DOR altered the market value, this should bear itself out with supporting market evidence. This Board cannot ignore the fact that Continental has sold a number of units in excess of the DOR’s determination of value, as illustrated in the following table:

Sale #	Sale Date	Sale Price	Unit Size (SF)	$/SF		DOR Value	DOR $/SF
1	2/14/02	$102,750	928	$110.72		$76,500	$82.44
2	2/27/02	$114,500	928	$123.38		$76,500	$82.44
3	7/31/02	$108,000	928	$116.38		$76,500	$82.44
4	7/31/02	$108,000	928	$116.38		$76,500	$82.44
5	9/30/02	$99,175	701	$141.48		$71,500	$102.00
6	9/30/02	$109,175	701	$155.74		$71,500	$102.00
7	11/4/02	$135,000	928	$145.47		$76,500	$82.44
8	12/10/02	$162,400	1168	$139.04		$84,000	$71.92
9	1/10/03	$112,500	928	$121.23		$76,500	$82.44
10	1/31/03	$108,000	928	$116.38		$76,500	$82.44
11	6/2/03	$112,000	701	$159.77		$71,500	$102.00
12	6/2/03	$121,000	928	$130.39		$76,500	$82.44
13	6/11/03	$105,000	701	$149.79		$71,500	$102.00
14	8/1/03	$113,000	928	$121.77		$76,500	$82.44
15	8/8/03	$121,000	928	$130.39		$76,500	$82.44
16	8/20/03	$121,000	928	$130.39		$76,500	$82.44
17	8/27/03	$116,000	928	$125.00		$76,500	$82.44
Garage		$7,500				$4,779	
Garage		$10,000				$4,779	

Based upon the DOR's value determination and the sales prices Continental obtained, the information in the above table suggests market values for single-family condominium property has increased significantly and exceeds that of an apartment complex.

The Taxpayer also asserts that once an individual unit is sold, a new market value would be established for tax purposes for that particular unit. This methodology would suggest the State of Montana employ individual acquisition value as a means of setting value for ad valorem tax purposes. This methodology is clearly in conflict with ***§15-7-112,MCA. Equalization of valuations.*** *The same method of appraisal and assessment shall be used in each county of the state to the end that comparable property with similar true market values and subject to taxation* *in Montana shall have substantially equal taxable values at the end of each cyclical revaluation program herein before provided* (emphasis supplied). Under this methodology, two identical units in this complex could have dramatically different values based solely on ownership. This would result in dissimilar taxes for two physically identical properties that receive the same services from the various taxing jurisdictions. The Board realizes that an individual sale price can reflect market value, but property within Class 4 is appraised on a six-year cycle.

Continental made the business decision to convert the property to condominiums, sell some of the units, and operate the balance as rental property. The Taxpayer also indicated that a number of the units would be sold until the property would cash flow. No one identified how many units this would require, nor is Continental precluded from selling all the units they have ownership of. In the process of appraising real property, the DOR must exclude Continental's business plan and look to what their responsibility is pursuant to Montana law. It's apparent by the sales prices that the values as condominiums far exceed that of an apartment complex. It appears as though the Taxpayer would have this Board value the property as a value in use. <u>The Appraisal of Real Estate</u>, Eleventh Edition, defines use value as, *the value a specific property has for a specific use. In estimating use value, the* *appraiser focuses on the value the real estate contributes to the enterprise of which it is a part, without regard to the property's highest and best use or the monetary amount that might be realized from its sale (24).* The highest and best use of the property was altered when the Taxpayer made the legal change. This Board must rely on §***15-8-111. Assessment -- market value standard -- exceptions.***

> *(1) All taxable property must be assessed at 100% of its market value except as otherwise provided.*
> *(2) (a) Market value is the value at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts.*
> *(3) The department may not adopt a lower or different standard of value from market value in making the official assessment and appraisal of the value of property.*
> *(c) as otherwise authorized in Titles 15 and 61.*

The Taxpayer originally sought a value of $6,100,000, the purchase price, but then modified its requested value to reflect the independent fee appraisal of $5,600,000. The independent fee appraisal is a valid indication of value for the property when it was appraised as an apartment complex. Statue, **§15-7-102 (6)** and **ARM 42.20.455**, both provide the consideration of an independent fee appraisal as determining market value. But the fact remains that the appraisal was for an apartment complex and the property was purchased as an apartment complex. Based on the conversion to condominiums and the sales prices that Continental is achieving, it's apparent that the highest and best use of the property is no longer apartment rental property. The Appraisal of Real Estate. Eleventh Edition, defines “Highest and Best Use” as, *“the reasonably probable and legal use of vacant land or an improved property, which is physically possible, appropriately supported, financially feasible, and the result in the highest value”.* After determining the highest and best use of a property, the analysis allows the appraiser the ability to identify property that is comparable to the property being appraised.

MCA §15-1-101. Definitions. *(e) The term “comparable property” means property that:*

(i) has similar use, function, and utility
(ii) is influenced by the same set of economic trends and physical, governmental, and social factors; and
(iii) has the potential of a similar highest and best use.

The value of the units as apartments suggests $54,901 per rental unit ($5,600,000/102). The sale prices clearly illustrate the highest and best use was conversion.

Neither party disputes that the property would require a fair amount of time to sell all 102 units. In fact the DOR’s DCF identified a sell-out period of seven years. In year 2002, Continental sold eight units, and in 2003, fifteen more units sold. Because it will require a period of time to sell all the units, it is the opinion of the Board that the best method in establishing the market value would be to employ a discounted cash flow analysis, or yield capitalization, recognizing the income from unit sales, income from unit rent, expenses associated with selling and operating rental property along with selecting an appropriate yield rate. The yield capitalization method would take into account the value of the units as condominiums and estimate an appropriate sell-out period, regardless of Continental's business plan.

As noted in the briefs filed by Continental, this issue of converting an existing apartment property into condominiums has been argued before various courts. The Supreme Court of Minnesota ruled in favor of a taxpayer that converted an apartment complex into individual condominiums, while renting the unsold units. In that decision the Court affirmed the decision of the lower Court, "*…The district court held that the taxpayer's property taxes on the unsold units should not have been based on the reassessed condominium value. On appeal, the court affirmed the judgment. The court determined that the Act provided for separate assessment and taxation of the individual condominium units. The court held that the legislature intended this separate treatment to begin when the unit was sold to a condominium purchaser…*" **Palatial Properties, Inc., v. County of Hennepin, 265 N.W.2d 207; (Minn., 1978).** Nothing was presented to this Board that suggests that Montana law provides the same treatment.

In Idaho, the Supreme Court ruled that the assessing authority must look beyond the condominium classification and consider the actual and functional use. **Fairway Development Company v. Bannock County, 750 P.2d 954; (Ida., 1988).**

The Board realizes that a sell-out period for the individual units would take an extended period of time. It is the Board's opinion that utilizing a discounted cash flow (DCF) analysis, recognizing that an estimated number of units would be sold each year and the remaining units would generate income as rental units. The Board afforded the parties an opportunity to present a DCF with supporting documentation. The following is the DOR's DCF.

DISCOUNTED CASH FLOW ANALYSIS

Examination of rental income as units sell-out:

Rents during Sell-Out Period	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Rental TTL
NOI (Hogan report)	504,336	504,336	504,336	504,336	504,336	504,336	504,336	
Adjusted rents (+ 5% Yr)	504,336	529,584	556,064	583,867	613,060	643,713	675,899	
7 Year Absorption Rates	1.0000	0.8571	0.7143	0.5716	0.4287	0.2858	0.1429	
Annual NOI	504,336	453,907	397,196	333,738	262,819	183,973	96,586	
Discount Factor @ 9% (PW1)	0.917431	0.841680	0.772183	0.708425	0.649931	0.596267	0.547034	
Discounted Cash Flows	462,721	382,044	306,708	236,428	170,814	109,697	52,836	1,721,249

Examination of unit sales during sell-out:

Unit Sell-Out Period	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Sales TTL
2002 DOR appraisal	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	
7 Year Absorption Rates	0.1429	0.1429	0.1429	0.1429	0.1429	0.1429	0.1429	
Annual Sales	1,134,297	1,134,297	1,134,297	1,134,297	1,134,297	1,134,297	1,134,297	
Adjusted sales (+ 5% Yr)	1,134,297	1,191,012	1,250,563	1,313,091	1,378,745	1,447,683	1,520,067	
Sales expenses @ 6%	68,058	71,461	75,034	78,785	82,725	86,861	91,204	
Property taxes (less 2001 taxes in Hogan's report expenses)	58,456	50,103	41,755	33,413	25,060	16,707	8,353	

Net Sales	1,007,783	1,069,448	1,133,774	1,200,893	1,270,960	1,344,115	1,420,510	
Discount Factor @ 9% (PW1)	0.917431	0.841680	0.772183	0.708425	0.649931	0.596267	0.547034	
Discounted Cash Flows	924,572	900134	875,481	850,742	826,037	801,451	777,067	5,955,484
							Cumulative Present Worth of Cash Flows:	**7,676,732**

The DOR's DCF utilized a seven-year sell-out period, or approximately fifteen units per year. Based upon the actual sales that have occurred that estimated period appears appropriate. The DOR recognized a net operating income in the first year of $504,336, which was taken from the Hogan report (pg. 54). The DOR in the first year of its DCF recognized selling off 14.29% of the property, or approximately 15 condominium units and 3 garages. The flaw that the Board identifies in the DOR's DCF is that one cannot collect rent for the entire year and in addition sell a portion of the complex, unless all transactions occurred December 31. The Board and the taxpayer identified this issue and the Board provided the DOR an opportunity to modify its DCF pursuant to an Order dated April 1, 2004. Sales of the condominium units will occur at different times throughout each year over the seven-year sellout period. It is the Boards opinion that an appropriate DCF should consider this and the DCF illustrated below analyzes the sellout period on a quarterly basis over a seven-year period.

The Board also requested that the DOR provide support for its determination of a 9% discount factor that was applied to both the rental and sales portions of the DCF. In its post-hearing submission the DOR responded as follows:

> The Hogan report provided evidence in support of a 9% capitalization rate. Discount rates may vary from market rendered direct cap rates, however; support is found for a 9% discount rate when valuing the more stable multi-family apartment categories in the INTEGRA REALTY RECOURCES REAL ESTATE INVESTMENT SURVEY – ROCKY MOUNTAIN REGION.

There are two problems with the DOR answer; first, in the eyes of the DOR the property is no longer a multi-family apartment complex and second, nothing from the Rocky Mountain survey accompanied their answer. It is the Board's opinion that there is additional risk associated with the sales of the individual condominium units. This additional risk can be experienced through interest rates, supply and demand for single-family housing, etc. The Taxpayer, in its post-hearing submission, suggested a discount factor of 12% to 13%. Like the DOR, the Taxpayer neglected to provide supporting documentation. It is the Board's opinion that an appropriate discount factor for the sales side of the DCF is 10%. This is also illustrated in the DCF below. In addition, the Board estimated property taxes illustrated on the DCF to be 1.5% of the established market value.

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DISCOUNTED CASH FLOW ANALYSIS

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
Rents during Sell-Out Period	Year 1- 1st Qtr	Year 1- 2nd Qtr	Year 1- 3rd Qtr	Year 1- 4th Qtr	Year 2- 1st Qtr	Year 2- 2nd Qtr	Year 2- 3rd Qtr	Year 2- 4th Qtr	Year 3- 1st Qtr	Year 3- 2nd Qtr	Year 3- 3rd Qtr	Year 3- 4th Qtr	Year 4- 1st Qtr	Year 4- 2nd Qtr	Year 4- 3rd Qtr	Year 4- 4th Qtr
Effective Gross Income (Hogan Report) with a 5% annual increase.	200,000	200,000	200,000	200,000	210,000	210,000	210,000	210,000	220,500	220,500	220,500	220,500	231,525	231,525	231,525	231,525
Expenses (Hogan Report) with a 5% annual increase & excluding property taxes.	56,700	56,700	56,700	56,700	59,535	59,535	59,535	59,535	62,512	62,512	62,512	62,512	65,637	65,637	65,637	65,637
NOI	143,300	143,300	143,300	143,300	150,465	150,465	150,465	150,465	157,988	157,988	157,988	157,988	165,888	165,888	165,888	165,888
7 Year Absorption Rates	0.9643	0.9286	0.8929	0.8571	0.8214	0.7857	0.7500	0.7143	0.6786	0.6429	0.6071	0.5714	0.5357	0.5000	0.4643	0.4286
Annual NOI	138,182	133,064	127,946	122,829	123,596	118,223	112,849	107,475	107,206	101,564	95,921	90,279	88,868	82,944	77,019	71,095
Discount Factor @ 9% (PW1)	0.917431	0.917431	0.917431	0.917431	0.841680	0.841680	0.841680	0.841680	0.772183	0.772183	0.772183	0.772183	0.708425	0.708425	0.708425	0.708425
Discounted Cash Flows	126,773	122,077	117,382	112,687	104,028	99,506	94,983	90,460	82,783	78,426	74,069	69,712	62,957	58,759	54,562	50,365
Examination of unit sales during sell-out:																
Unit Sell-Out Period	Year 1- 1st Qtr	Year 1- 2nd Qtr	Year 1- 3rd Qtr	Year 1- 4th Qtr	Year 2- 1st Qtr	Year 2- 2nd Qtr	Year 2- 3rd Qtr	Year 2- 4th Qtr	Year 3- 1st Qtr	Year 3- 2nd Qtr	Year 3- 3rd Qtr	Year 3- 4th Qtr	Year 4- 1st Qtr	Year 4- 2nd Qtr	Year 4- 3rd Qtr	Year 4- 4th Qtr
2002 DOR appraisal	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700
7 Year Absorption Rates	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357
Quarterly Sales	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489
Adjusted sales (+ 5% Yr)	283,489	283,489	283,489	283,489	297,664	297,664	297,664	297,664	312,547	312,547	312,547	312,547	328,174	328,174	328,174	328,174
Sales expenses @ 6%	17,009	17,009	17,009	17,009	17,860	17,860	17,860	17,860	18,753	18,753	18,753	18,753	19,690	19,690	19,690	19,690
Property taxes : 1.5% of the 2002 reappraised value.	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400
Net Sales	240,080	240,080	240,080	240,080	253,404	253,404	253,404	253,404	267,394	267,394	267,394	267,394	282,084	282,084	282,084	282,084
Discount Factor @ 10% (PW1)	0.909091	0.909091	0.909091	0.909091	0.826446	0.826446	0.826446	0.826446	0.751315	0.751315	0.751315	0.751315	0.683013	0.683013	0.683013	0.683013
Discounted Cash Flows	218,255	218,255	218,255	218,255	209,425	209,425	209,425	209,425	200,897	200,897	200,897	200,897	192,667	192,667	192,667	192,667

	17	18	19	20	21	22	23	24	25	26	27	28	
Rents during Sell-Out Period	Year 5- 1st Qtr	Year 5- 2nd Qtr	Year 5- 3rd Qtr	Year 5- 4th Qtr	Year 6- 1st Qtr	Year 6- 2nd Qtr	Year 6- 3rd Qtr	Year 6- 4th Qtr	Year 7- 1st Qtr	Year 7- 2nd Qtr	Year 7- 3rd Qtr	Year 7- 4th Qtr	
Effective Gross Income (Hogan Report) with a 5% annual increase	243,101	243,101	243,101	243,101	255,256	255,256	255,256	255,256	268,019	268,019	268,019	268,019	
Expenses (Hogan Report) with a 5% annual increase & excluding property taxes.	68,919	68,919	68,919	68,919	72,365	72,365	72,365	72,365	75,983	75,983	75,983	75,983	
NOI	174,182	174,182	174,182	174,182	182,891	182,891	182,891	182,891	192,036	192,036	192,036	192,036	
7 Year Absorption Rates	0.3929	0.3571	0.3214	0.2857	0.2500	0.2143	0.1786	0.1429	0.1071	0.0714	0.0357	0.0000	
Annual NOI	68,429	62,208	55,987	49,766	45,723	39,191	32,659	26,127	20,575	13,717	6,858	0	
													Rental TTL
Discount Factor @ 9% (PW1)	0.649931	0.649931	0.649931	0.649931	0.596267	0.596267	0.596267	0.596267	0.547034	0.547034	0.547034	0.547034	
Discounted Cash Flows	44,474	40,431	36,388	32,345	27,263	23,368	19,474	15,579	11,255	7,504	3,752	0	**$1,661,360**
Examination of unit sales during sell-out:													
Unit Sell-Out Period	Year 5- 1st Qtr	Year 5- 2nd Qtr	Year 5- 3rd Qtr	Year 5- 4th Qtr	Year 6- 1st Qtr	Year 6- 2nd Qtr	Year 6- 3rd Qtr	Year 6- 4th Qtr	Year 7- 1st Qtr	Year 7- 2nd Qtr	Year 7- 3rd Qtr	Year 7- 4th Qtr	
2002 DOR appraisal	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	7,937,700	
7 Year Absorption Rates	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	0.0357	
Quarterly Sales	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	283,489	
Adjusted sales (+ 5% Yr)	344,583	344,583	344,583	344,583	361,812	361,812	361,812	361,812	379,903	379,903	379,903	379,903	
Sales expenses @ 6%	20,675	20,675	20,675	20,675	21,709	21,709	21,709	21,709	22,794	22,794	22,794	22,794	
Property taxes : 1.5% of the 2002 reappraised value.	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	26,400	
Net Sales	297,508	297,508	297,508	297,508	313,703	313,703	313,703	313,703	330,709	330,709	330,709	330,709	
													Sales TTL
Discount Factor @ 10% (PW1)	0.620921	0.620921	0.620921	0.620921	0.564474	0.564474	0.564474	0.564474	0.513158	0.513158	0.513158	0.513158	
Discounted Cash Flows	184,729	184,729	184,729	184,729	177,077	177,077	177,077	177,077	169,706	169,706	169,706	169,706	**$5,411,022**

Cumulative Present Worth of Cash Flows: **$7,072,381**

The market value as a result of the Board's DCF shall be applied to the subject property as follows:

Total DCF value	$7,072,381
Less land value (102 unit @ $15,000 per Unit)	$1,530,000
Improvement value	$5,542,381
Less garage value (24 units @ $4,750 per Unit)	$114,000
Total condominium value	$5,428,381

One bed SF		701	$ per SF	Total One Bedroom Units	One Bedroom Unit Value	Land Value per Unit	**Total Unit Value**
8 units		8					
Total SF		5,608	$57.29	$321,257	$40,157	$15,000	**$55,157**
Two bed SF		928		Total Two Bedroom Units	Two Bedroom Unit Value		
	86	86					
Total SF		79,808	$57.29	$4,571,847	$53,161	$15,000	**$68,161**
Three bed SF		1,168		Total Three Bedroom Units	Three Bedroom Unit Value		
8 units		8					
Total SF		9,344	$57.29	$535,276	$66,910	$15,000	**$81,910**
Total Condo SF		94,760					
Allocated $ per SF ($5,428,381/94,760 SF)			$57.29				

CONCLUSIONS OF LAW

1. The Board has jurisdiction over this matter in accordance with Section 15-2-301, MCA.
2. The subject property is classified as Class Four condominium subject to individual assessment pursuant to §15-8-511, MCA.
3. The Board shall give an administrative rule full effect unless the Board finds a rule arbitrary, capricious or otherwise unlawful. Section 15-2-301(4), MCA.

4. (Western Airlines, Inc., v. Catherine Michunovich et al., 149 Mont. 347, 428 P.2d 3, (1967)
5. §15-7-111, MCA. Periodic revaluation of certain taxable property.
6. §15-7-112,MCA. Equalization of valuations.
7. §15-8-111. Assessment -- market value standard -- exceptions.
8. The appeal of the Taxpayer in hereby denied, but the decision of Missoula County Tax Appeal Board is modified.

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ORDER

IT IS THEREFORE ORDERED by the State Tax Appeal Board of the State of Montana that the property in question is properly classified as Class Four condominium subject to individual assessment pursuant to §15-8-511 MCA. The proportionate share of the land and individual condominium units, along with the garages is valued as follows:

One Bedroom Condominium with land:	$55,157
Two Bedroom Condominium with land:	$68,161
Three Bedroom Condominium with land:	$81,910
Individual Garage	$ 4,750

DATED this 12th day of May, 2004.

BY ORDER OF THE
STATE TAX APPEAL BOARD

(S E A L)

____
GREGORY A. THORNQUIST, Chairman

____
JEREANN NELSON, Member

____
JOE R. ROBERTS, Member

NOTICE: You are entitled to judicial review of this Order in accordance with Section 15-2-303(2), MCA. Judicial review may be obtained by filing a petition in district court within 60 days following the service of this Order.

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on this 12th day of May, 2004, the foregoing Order of the Board was served on the parties hereto by depositing a copy thereof in the U.S. Mails, postage prepaid, addressed to the parties as follows:

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