

**701—102.5(421,428,441) Valuation of commercial real estate.** Commercial real estate shall be assessed at its actual value as defined in Iowa Code section 441.21. In determining the actual value of commercial real estate, city and county assessors shall use the appraisal manual issued by the department of revenue pursuant to Iowa Code section 421.17(17) as well as a locally conducted assessment/sales ratio study, an analysis of sales of comparable properties, and any other relevant data available. In cases involving the valuation of owner-occupied commercial property, the data relating to the financial performance of the owner or the owner's business, including but not limited to its sales, revenue, expenses, or profits, shall not be considered relevant in determining the property's actual value.

**102.5(1) Property of long distance telephone companies.** The director of revenue shall assess the property of long distance telephone companies as defined in Iowa Code section 476.1D(10) which property is first assessed for taxation on or after January 1, 1996, in the same manner as commercial real estate.

**102.5(2) Low-income housing subject to Section 42 of the Internal Revenue Code.**

*a. Productive and earning capacity.* In assessing property that is rented or leased to low-income individuals and families as authorized by Section 42 of the Internal Revenue Code which limits the amount that the individual or family pays for the rental or lease of units in the property, the assessor shall use the productive and earning capacity from the actual rents received as a method of appraisal and shall take into account the extent to which that use and limitation reduces the market value of the property.

*b. Direct capitalization method.* The income approach to valuation shall be applied using the direct capitalization method. The assessor may use the discounted cash flow method as a test of the reasonableness of the results produced by the direct capitalization method. The direct capitalization method of the income approach involves dividing the Net Operating Income (NOI) on a cash basis by an overall capitalization rate to derive an indication of the value of the property for the assessment year.

In applying the direct capitalization method, the assessor shall develop a normalized measure of annual NOI based on the productive and earning capacity of the development utilizing (1) the actual rent schedule applicable for each of the available units as of January 1 of the year of assessment indicating the actual rent to be paid by the resident plus any Section 8 rental assistance or other direct cash rental subsidy provided to the resident by federal, state or local rent subsidy programs as limited pursuant to Section 42 of the Internal Revenue Code, (2) a normal vacancy/collection allowance, (3) the prior year's actual and current year's projected annual operating expenses associated with the property, excluding noncash items such as depreciation and amortization, but including property taxes and those actual costs expected to be incurred and paid as required by Internal Revenue Code Section 42 regulations, provisions, and restrictions as applicable to the assessment year, and (4) an appropriate provision for replacement reserves.

If no separate line item is included for reserves for replacement in the historic income and expense data, then the maintenance and repair categories of the historic expense data must be itemized. For properties that have attained a normalized operating history, the NOI results of the prior three years (as represented in the statements variously named as the Income and Loss Statement, the Profit and Loss Statement, the Income Statement, the Actual to Budget Comparison Statement, Balance Sheet, or some name variation of these) may be used to provide the basis for determining the normalized NOI used for purposes of applying the direct capitalization method for the year of assessment, provided an appropriate replacement reserve is included in the NOI determination and provided any additional costs required as a result of Section 42 regulation or compliance changes for the assessment year are included as an operating expense in the NOI determination. In addition, the assessor may utilize the current year operating budget to develop a measure of NOI for the assessment year. The assessor, in developing the measure of annual NOI on a cash basis, shall not consider as income any potential rental income differential that could otherwise be received from the property if the rents were not limited pursuant to Section 42 of the Internal Revenue Code, any tax credit equity, any tax credit value, or other subsidized financing.

*c. Filing of reports.* It shall be the responsibility of the property owner to file income and expense data with the local assessor by March 1 of each year. The assessor may require the filing of additional information if deemed necessary.

*d. Capitalization rate.* The overall capitalization rate to be used in applying the direct capitalization method for a Section 42 property is developed through the band-of-investment technique. The capitalization rate will be calculated annually by the Iowa department of revenue and distributed to all Iowa

assessors by March 1. The capitalization rate is a composite rate weighted by the proportions of total property investment represented by debt and equity. The capital structure weights equity at 80 percent and debt at 20 percent unless actual market capital structure can be verified to the assessor. The yield, or market rate of return, for equity is calculated using the capital asset pricing model (CAPM). The yield for debt is equivalent to the average yield on 25-year Treasury bonds referred to as the Treasury long-term average rate. An example of the band-of-investment technique to be utilized is as follows:

	% to Total	Yield	Composite
Equity	80%	11.05%	8.84%
Debt	20%	5.94%	1.19%
	100%		10.03%

*e. Capital asset pricing model.* The capital asset pricing model (CAPM) is utilized to develop the equity rate. The formula is:

$$Re = B(Rm - Rf) + Rf$$

Where: Re = return on equity  
 B = beta  
 Rm = return on the market  
 Rf = risk-free rate of return  
 Rm - Rf = market-risk premium

The beta is assumed to be 1 which indicates the risk level to be consistent with the market as a whole. The risk-free rate is calculated by finding the average of the three-month and six-month Treasury bill. The return on the market is calculated by taking the average of the return on the market for the Merrill Lynch Universe and Standard and Poor's 500 or by reference to other published secondary sources.

*f. Properties under construction.* For Section 42 properties under construction, the assessor may value the property by applying the percentage of completion to the replacement cost new (RCN) as calculated from the Iowa Real Property Appraisal Manual and adding the fair market value of the land. Alternatively, projected income and expense data may be utilized if available.

*g. Negative or minimal NOI.* If the Section 42 property shows a negative or minimal net operating income (NOI), the indicator of value as set forth in these rules shall not be utilized.

*h. Eligibility withdrawn.* The property owner shall notify the assessor when property is withdrawn from Section 42 eligibility under the Internal Revenue Code. The notification must be provided by March 1 of the assessment year or the owner is subject to a penalty of \$500.

This rule is intended to implement Iowa Code sections 421.17, 428.4, 441.21 as amended by 2004 Iowa Acts, Senate File 2296, and 476.1D(10).

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