Dangerous Implications of Assessor Overreach

What is the problem?

Is retail property really being over assessed?
Yes. Assessors are using the cost approach (construction cost) as well as subjective criteria when valuing property. Retailers are appealing property tax assessments because their property is being overvalued using methods that do not reflect the property's true cash value.

Large, freestanding retail stores are built to suit the owner's nationally recognized footprint and layout. These buildings have less value to another retailer, who would choose to reimage the property to fit its business model. The Michigan Tax Tribunal agrees: "first generation users develop big box retail space to enhance retail sales and not to optimize market value to the property."[1]

What is the real problem locals are trying to solve?
The real problem is lack of funding: the state has reduced revenue sharing payments to local governments while local units have been forced to realize previously unfunded liabilities of pension payments and "Cadillac" retiree healthcare plans. Local governments are now encouraging assessors to overstep their boundaries and assess business property at a higher rate in order to pay for their government operations and benefits without "harming communities." There needs to be accountability for overreaching local assessors and their employers.

Is there a problem with Michigan law that needs to be addressed?
No. Michigan law defines true cash value of a building and its adjacent property as what the physical property is worth to a new buyer. The law also provides a clear process for all property owners to contest assessments if they feel the property was unfairly assessed.

How is property assessed in Michigan?

What is True Cash Value (TCV) and how is it determined?
The true cash value of a building and its adjacent property is what the physical property is worth to a new buyer. The Michigan Legislature defines True Cash Value (TCV) as the usual selling price (MCL 211.27(1)). The Michigan Supreme Court has determined "[t]he concepts of 'true cash value' and 'fair market value' . . . are synonymous."[2]

How do assessors determine TCV?
The law and courts generally accept three approaches to determine TCV: the sales comparison or market approach, the capitalization-of-income approach, and the cost-less-depreciation approach. The sales comparison approach relies on comparable sales of similar property. The capitalization-of-income approach is used for income-producing properties and relies on market rent. The cost-less-depreciation approach relies on the estimated value of the land and the estimated cost (less depreciation) of the improvements and considers the reproduction cost and/or replacement cost.

Is the cost approach a correct approach to assess retail property?
No. Potential buyers do not place any reliance on the original construction cost to the original owner. That faulty logic would assume that a home built for $2 million will always be worth $2 million to every buyer. "Each big box store retailer has its own business image and desired store layout and design – façade, flooring, lighting, location of restrooms, etc. [Each retailer] wants all its stores to look alike and not like another retailer's stores."

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1 *Mernard Inc. v City of Escanaba*, MTT Docket 441600, (2014)
2 *CAF Investment Co v Michigan State Tax Comm*, 392 Mich 442, 450; 221 NW2d 588 (1974)

What is Highest and Best Use (HBU)?
Highest and best use is a "principle of appraisal and assessment requiring that each property be appraised as though it were being put to its most profitable use (highest possible present net worth), given probable legal, physical, and financial constraints. The principle entails first identifying the most appropriate market, and, second, the most profitable use within that market."[3]

What do the experts say?

What do the Michigan Tax Tribunal, Michigan Court of Appeals, and Michigan Supreme Court have to say on the matter?
Retailers appealing faulty assessments based on the cost approach or subjective criteria have routinely prevailed at the Michigan Tax Tribunal and the Michigan Court of Appeals. The Michigan Supreme Court refused to hear a 2014 appeal on the basis that there was no need to review the Court of Appeals decision.

Which approach does the Michigan Tax Tribunal most often recommend for retail property?
The Michigan Tax Tribunal has repeatedly found that the sales comparison approach is the most accurate and fair way of valuing original owner-occupied retail buildings. The income approach may be used for valuation but is not as reliable as the sales comparison approach. The Michigan Tax Tribunal agreed with a petitioner who stated that the "cost approach is given no weight or credibility in the determination of market value" and is "not relevant or necessary because potential buyers do not place any reliance on this approach."[4]

Can assessors use the identity of the current owner to determine Highest and Best Use (HBU)?
No. While the use of the property as a big box store is valid, the identity of the owner is irrelevant. "[T]he constitution and the [General Property Tax Act] require that property tax assessments be based on market value, not value to the owner."[5] An assessor is not tasked with determining the market value of a certain branded store but rather the market value of a big box building.

Do negative use restrictions – or deed restrictions – impact the sale price of a property?
Maybe. Similar to a zoning restriction, a deed restriction may or may not affect market value. A number of factors impact the market-selling price of a property and it is the assessor's job to consider all of those factors when determining valid comparable sales.

What does the proposed solution accomplish?

Why do local governments want to change the definition of true cash value?
Their motivation is simply a money grab. Local governments are blaming retailers for lost revenue rather than the state's revenue sharing cuts and their own broken budgets. Local government officials should focus on developing an economically viable community rather than imposing higher taxes on retailers through inflated, illegal assessments.

Why do local governments want to change the definition of true cash value for some taxpayers but not others?
Local government officials believe it is easier to tack on higher taxes to businesses rather than individual taxpayers. It is clear that this will not stop with large retailers; associations representing local units of government have admitted: "the area in greatest need of reform is property taxes."[6] The Michigan Municipal League goes on to suggest: "Michigan needs to change from a 'cut only' approach to balancing

3 International Association of Assessing Officers, *Glossary for Property Appraisal and Assessment*, Second Edition, http://www.iaao.org/media/Pubs/IAAO_Glossary.pdf, Accessed 9/24/15
4 *Mernard Inc. v City of Escanaba*, MTT Docket 441600, (2014)
5 *First Fed S&L Ass'n of Flint v City of Flint*, 415 Mich 702, 703; 329 NW2d 755 (1982)
6 Minghine, Anthony, "Funding for the Future," *The Review the official magazine of the Michigan Municipal League*. May/June 2015, p 7.

budgets, to one of investing in [communities]."[7] "The solutions do exist. Among them: more local tax options. A balanced distribution of revenue sharing funds for communities with a higher tax effort or higher legacy costs. Reform the system of property tax assessment and appeal."[8]

Is it constitutional?
The Michigan Constitution requires that true cash values be uniformly set. Making presumptions on how true cash value is determined for one type of property over another would violate the constitutional principle set forth in Article IX, Sec. 3.[9]

What impact would proposed legislation have on retailers and other property owners?

Would proposed legislation give local units of government the power to take retail property?
Yes. This dangerous proposal would allow local governments to condemn retail property that remained vacant for more than 90 days through the Blighted Area Rehabilitation Act.

Does this raise taxes?
Yes. The legislation seeks to dramatically increase the value of a building to its original construction costs, which are not relevant in the market sale of property. A potential buyer would require significant modifications to the property, which limits the market value. The increase would double property taxes on retail businesses while inflating the valuation to a level that will never be recuperated if the property is sold.

Could this impact homeowners and small businesses?
Yes. This proposal is a slippery slope that could easily lead to changes for homeowners and small businesses. A change of this proportion would set a precedent for other property, since Michigan's constitution requires that real and personal tangible property be taxed uniformly.[10]

For example, relying on the cost approach for homeowners in an area with few residential sales would artificially inflate the value of the property in an unfair manner. Current property value is not the same as the replacement cost of the property. "The market approach is the only valuation method that directly reflects the balance of supply and demand for property in marketplace trading."[11]

What impact would proposed legislation have on Michigan's economy?

What impact would this have on retailers looking to come to Michigan?
A subjective change in property tax valuations would likely deter non-Michigan based retailers from opening stores in Michigan.

Could this impact retail jobs?
Yes. Retail profit margins are thin, typically less than 2 percent. A significant increase in property taxes could impact the number of employees a retailer can keep on the payroll. Retail jobs make up over 10 percent of Michigan's job market. (Our Buy Nearby materials say nearly 1 in 4 ... where did 10 percnt come from?)

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7 Minghine, Anthony, "Funding for the Future," *The Review the official magazine of the Michigan Municipal League.* May/June 2015, p 7.
8 Philips Foley, Elizabeth, "Fixing Municipal Finance," *The Review the official magazine of the Michigan Municipal League,* May/June 2015, p 14.
9 *The Michigan Constitution,* Article IX, Sec. 3
10 *The Michigan Constitution,* Article IX, Sec. 3
11 *Jones & Laughlin Steel Corp, supra* at 353 (citing *Antisdale, supra at 276 n 1*)