Property tax basics for business: Make sure you're not paying too much

BY R. WILSON MONTJOY II AND ROBERT M. MEGGINSON

Property taxes can be a significant annual expense. It is therefore important to ensure that the annual bill is appropriate, and the taxpayer does not pay more than is legitimately owed. This article will provide a refresher on the basics of the tax process and then highlight several areas of inquiry to verify the accuracy of the annual bill.

Property taxes (or ad valorem taxes) are a local tax designed to support county, city and school district budgets. The principal participants in the annual process are also local.

The local tax assessor annually determines the value of all taxable real and personal property in the county (with the exception of utility property which is assessed by the State Tax Commission). Typically, the county assessor acts on behalf of both the county and city. The board of supervisors, city council and school district each set an annual tax rate (called the millage rate) sufficient to meet budget needs based on the total assessed value. Finally, the tax collector computes and issues tax bills, handles the collection process and conducts an annual tax sale of properties for which taxes have not been paid.

The annual tax process begins with an assessment by the tax assessor, who determines the true value of all taxable property as of January 1. "True value" is statutorily defined to mean and include, "market value, cash value, actual cash value, proper value and value for the purposes of appraisal for ad valorem taxation." Wherever possible, the assessor is to consider the three traditional appraisal approaches to value – income, cost and market data.

For personal property, valuation includes a rendition to be filed by April 1 by the taxpayer, which lists taxable personal property and its true value. If a rendition was filed in a previous year, most counties request that the taxpayer simply show changes (additions or deletions) from the prior year's rendition. In the rendition, the taxpayer is to estimate true value at the time of valuation (normally January 1), not a "forced sale" price, but "what he would be willing and would expect to accept for it if he were disposed to sell it." The Mississippi State Tax Commission rules provide that the base for industrial property will be original acquisition cost new, adjusted for inflation and depreciation. For business property, the tax commission pricing guide is the source of value, and is then adjusted for inflation. The rules also provide for consideration of functional and economic (external) obsolescence.

By the first Monday in July, the tax assessor should have completed the real and personal tax rolls and turned them over to the board of supervisors. During July, the board reviews the rolls and equalizes the assessments. Absent a disagreement, the rolls are then sent to the State Tax Commission for review. After tax commission review, the rolls are finalized and tax bills are issued typically in December. Payment is due on or before February 1 of the following year, unless the taxpayer elects to pay in installments – _ by February 1, _ by May 1 and _ by July 1.

If taxes are not timely paid, interest accrues at the rate of 1 percent per month and the property may ultimately be sold to delinquent taxes. Most counties hold the annual tax sale beginning on the last Monday in August. If your property is sold at a tax sale, all is not lost – the taxpayer has two years before title vests in the tax sale purchaser redeem the property by paying the delinquent expenses and 1 _ percent per month.

Because taxes are levied based upon the property's value, an overassessment will result in an excessive tax bill. The first step to redress an excessive valuation is to raise the issue with the local tax assessor prior to the first Monday in July, when the assessor is obligated to complete the real and personal tax rolls and turn them over to the board of supervisors. During July, the board reviews the tax rolls and, in August, the taxpayer must protest the assessment or be foreclosed (except for certain defects noted below). If the taxpayer's protest is not granted by the board, the next step is an appeal to the circuit court.

If the taxpayer fails to protest in August as described above, there are fourteen specific circumstances listed by statute for which a taxpayer may challenge and the board may revise an assessment up to the last Monday of the next year. Examples of the qualifying defects include: a double assessment, a clerical or mathematical error, an assessment to the wrong person, an assessment of property that does not exist or is exempt, or an assessment for more than "actual value" based upon the affidavits of two competent witnesses.

The process to value property is complex, and a complete listing of all areas of possible challenge is beyond the scope of this article. However, some examples are listed below.

Lien date Taxes are a lien as of January 1, and the assessment is based upon the property's true value and use as of that date. Events occurring after January 1 should not be considered in the current year. Thus, a building, which was not completed until June, or manufacturing and machinery equipment not placed into service until June is generally not subject to tax that year. Conversely, property conveyed in June to an exempt entity like a church is subject to tax because the owner on January 1 was not exempt.

Age and size Basic information, such as age and square footage are significant in determining value. Thus, an error in the size of a building can result in an incorrect assessment. Verifying the accuracy of the assessor's records regarding size, type of construction, age, etc., is a relatively simple step the taxpayer can take to help ensure accuracy.

Mass Appraisal vs. Fee Appraisal Although value is determined each year, no assessor has the time or manpower to individually appraise each property each year. Consequently, appraisers use a system called mass appraisal to determine value. Mass appraisal is a systematic appraisal of groups of properties as of a given date using standardized procedures and statistical testing. The other method of determining value, fee appraisal, is a process in which one hires a qualified real estate appraiser to value a single property as of a given date. Both approaches have their place and both have safeguards to assure accuracy. However, for a taxpayer who is only interested in a single property, there are possible shortcomings with mass appraisal. One fundamental difference is that the statistical measures used to determine the accuracy of mass appraisal approach essentially determine whether, on average, properties are being fairly assessed. Naturally, any average can disguise the fact that individual properties may be significantly over or under assessed. It is this deviation that an individual fee appraisal may reveal, and it is this distinction that a taxpayer should be on the look out for. Additionally, mass appraisal is best used for typical properties, and finds its greatest shortcomings when applied to unusual or special use property. Particular care should be taken to determine whether the mass appraisal variant of the cost approach correctly captures the value of property like manufacturing machinery and equipment.

Obsolescence Mass appraisal approaches typically do not consider depreciation except in accordance with standard tables produced by the State Tax Commission. However, there are instances in which property has suffered excess obsolescence that justifies significantly increased depreciation. Examples include:

(1) Excessive physical deterioration;

(2) Functional obsolescence – an impairment in value caused by new inventions, changes in design, improved production processes, poor or inappropriate architecture, lack of modern equipment, inappropriate or wasteful floor plan, etc; and

(3) Economic or external obsolescence – an impairment caused by external factors such as external market conditions, zoning, neighborhood decline, or governmental actions.

State Tax Commission rules do allow for assessors to consider the granting of additional depreciation, but require proof on a case-by-case basis. Taxpayers should be sensitive to instances in which any of the foregoing can be demonstrated to justify increased depreciation.

Environmental Contamination Properties that have been contaminated may suffer diminished value in a number of ways, each of which may be considered to reduce the assessed value of properties. For example, some or all of the cost of remediation to comply with the order of an environmental regulator may be deducted from the value of the property in appropriate circumstances. Additionally, the consequences of environmental contamination may even affect the available use or profitability of property, which should also be considered. Finally, property that has not been contaminated but is adjacent to contaminated properties may suffer a "stigma" that affects the value and may be properly considered in reducing the assessments.

Salvage Value State Tax Commission Rules provide for a 90% depreciation factor to property which has been removed from use and been declared as salvage property. However, since the assessor may not visit each industrial property each year, it is incumbent upon the taxpayer to make the assessor aware of this change of use in its annual rendition.

Taxable vs. Nontaxable Property For large, special use properties, like manufacturing facilities, the improvements and personal property are typically valued based on taxpayer's self-reported cost of construction or acquisition. However, the taxpayer making its April 1 rendition should be careful because not all property capitalized on the company's books is taxable. Typically, "soft costs" such as interest during construction is not taxable. Also, improvements that are actually owned by another taxpayer, such as a utility connection owned by the local utility but paid for by the taxpayer, should be excluded.

Exemptions Some taxpayers are unaware that economic development exemptions may be granted for certain activities. For example, new manufacturing enterprises or expansions of existing enterprises may be granted an exemption by local governing authorities of a portion of the annual property tax liability (usually around _) for up to ten (10) years. Similarly, expansions of existing facilities may be granted exceptions. Additionally, a freeport warehouse exemption may be used to completely exempt the value of goods in storage or manufactured goods on site, which are destined for shipment out of state. Likewise, goods in federally designated ports that are in transit may be completely exempt from taxation. One problem is that the exemption statutes are scattered throughout the Mississippi Code and are not always easy to understand and apply. The advice of a practitioner in the area may be necessary to ascertain what exemptions may be available. Additionally, the Mississippi State Tax Commission Website contains a good summary of exemptions at www.mstc.state.ms.u./revebye/main.htm. **DBJ**

(R. Wilson Montjoy II is a member of Brunini Grantham Grower & Hewes. He maintains a significant practice in the area of ad valorem taxation and state and local tax incentives and may be contacted at 601-960-6856 or wmontjoy@brunini.com. Robert M. Meginnson is the former head of the Office of Property Tax of the Mississippi State Tax Commission, and currently a Property Tax Consultant with Brunini. He may be contacted at 601-973-8702 or rmegginson@brunini.com.)