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U.S. MASTER™ PROPERTY TAX GUIDE

Wolters Kluwer

2016
U.S. Master™ Property Tax Guide

Wolters Kluwer Editorial Staff Publication

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PREFACE

This *2016 U.S. Master™ Property Tax Guide* is designed as a quick-reference work for property taxes as imposed by state and local taxing authorities. The *Guide* presents a general state-by-state picture of these taxing authorities that is useful to tax practitioners, businesspersons, and others who prepare and file property tax returns or are required to deal with such taxes.

The *Guide* reflects legislative changes made through December 2015.

The Overview (Property Tax Basics) section provides a synopsis of property tax concepts, property tax cycles, local tax administration, assessments of property, the setting of tax rates, and the payment of taxes. The arrangement of the state summaries is uniform from state to state, simplifying the reference of specific topics across states.

The *Guide* is not designed to eliminate the necessity of referring to the law and regulations for definitive answers to complicated problems. For the text of state tax laws and regulations, as well as a more comprehensive discussion of the various state and local property tax systems, consult the CCH state tax reporters.

February 2016

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OVERVIEW

Property Tax Basics

For purposes of this *Guide,* a property tax is considered to be a tax on property measured by the property's value as of a specified date. Because this type of tax is assessed according to the value of property, it is commonly referred to as an *ad valorem* (Latin for "according to value") tax. In addition, a property tax can be considered a direct tax in that it applies to the property itself, as compared to the right to enjoy the property or to any income that may be derived from its ownership or use.

Among the oldest types of tax, the property tax at one time was the main source of revenue for most states. However, the advent of state income and sales taxes significantly reduced the fiscal importance of property taxes to state governments. In most states today, property taxes are relied upon most heavily by counties, municipalities, school districts, and other local governmental units as their primary source of revenue.

• Property tax cycle

Property taxes are levied on an annual basis that generally corresponds to the fiscal year of the jurisdiction imposing the tax. However, the process of determining how much tax each property owner owes generally commences anywhere from nine to 18 months before the tax bills are mailed, depending on the state. Given the importance of property tax revenues to local budgets, each assessment cycle includes fairly strict deadlines for completing each of the acts that are necessary to levy the tax.

The amount of property tax levied on a given item of property is typically a function of the following two factors: (1) the total of the tax rates that have been set by the various governmental bodies that have the authority to tax the property; and (2) the taxable value of the property. The tax base is determined through the assessment process, which entails first identifying all taxable property located within a taxing jurisdiction and then establishing the taxable value of that property by state and/or local assessors. Once an assessor has set a taxable value for a property, the owner has a window of opportunity to contest that value before it becomes fixed for the current tax year.

After the taxable values have been established and, in some cases, officially certified by state or local equalization boards, the tax is levied through the setting of local tax rates. Because property tax revenues generally comprise a significant portion of a taxing jurisdiction's budget, the tax rate commonly becomes a function of the total tax base and revenue needs of each jurisdiction.

After the tax has been levied, the final stage in the property tax cycle is the payment and, if necessary, enforced collection of the taxes levied.

• Tax administration

Although local officials typically handle most of the property tax assessment and collection activity, that activity is largely governed by state constitutional and statutory provisions and is overseen to various degrees by state-designated agencies. This is a natural consequence of the common state constitutional requirement that the taxation of property within a state be uniform.

State role: Apart from laying the general statutory foundation for the assessment and collection of property taxes, state agencies usually have a rather limited role in the day-to-day administration of property taxes. The agency vested with the responsibility for carrying out the state functions, whether it is a department of revenue or taxation, comptroller's office, or distinct state board of equalization, primarily serves a supervisorial role by monitoring and regulating local assessment practices, participating in the equalization of assessments, and advising localities and taxpayers on property tax issues.

In most states, however, the state does assume the responsibility for assessing certain types of property that for one reason or another do not lend themselves to local assessments. The most common type of centrally assessed property across the states is property owned by public utilities. Other examples of property that may be centrally assessed in a particular state are intangible property, mining and other natural resource property, and business inventories.

Local role: A local assessor performs the primary functions in assessing the property tax. In most states, the assessor, who, depending on the jurisdiction, may be either an elected or appointed official, operates on a county level, with city, town, and/or municipal officials acting in only about one-fourth of the states. An assessor's general role is to identify and inventory all assessable property in the jurisdiction, appraise the taxable property, and enroll the property on the local assessment roll. The nature of these activities also necessitates that the assessor maintain property records to support the timeliness and accuracy of assessment.

Once the assessor has finalized the local assessment roll, which essentially represents the available tax base for the jurisdiction, the roll is generally subject to review by a local, regional, or state body (commonly identified as a board of equalization or board of review). That body bears the responsibility of raising or lowering any incorrect valuations, adding any property to the roll that the assessor may have improperly or inadvertently omitted, and otherwise correcting other apparent errors such as property descriptions or classifications. The body also usually serves as the first stop in the official appeals process for taxpayers desiring to contest the valuation or classification of their property.

Upon certification of the assessment roll by the review board, the final property values are allocated back to the appropriate taxing jurisdictions, which determine the actual tax amount on the basis of their annual budgetary requirements. The collection of the tax owed by property owners and the distribution of the tax receipts to the appropriate local jurisdictions are usually performed by local tax collectors and tax auditors, respectively.

Assessment of Property

The assessment of property for property tax purposes essentially requires assessors to answer two basic questions for each item of property within their taxing district. First, is the property taxable? Second, if the property is taxable, what is its taxable value?

Assessment date: The assessment date is usually seen as the beginning of the property tax cycle. Ownership of the property, how the property is used, and market conditions as of that date generally establish whether the property is taxable and, if so, at what value it is taxed and who becomes liable for paying the tax. Although property that is not located within a taxing jurisdiction on the assessment date generally is not subject to tax, exceptions to this rule are frequently made with respect to mobile property and to property under construction.

- **What property is taxable?**

State property tax systems typically follow one of two schemes: (1) that all property, without enumeration, is taxable unless specifically exempt; or (2) that only such classes of property as are specifically enumerated are taxable. In either case, real property (called "immovable property" in Louisiana) forms the backbone of every property tax system, as such property is taxable in every state in the absence of an applicable exemption.

At least some tangible personal property ("movable property" in Louisiana) is taxable in nearly every state. Only in Delaware, Hawaii, Illinois, Iowa, New York, and Pennsylvania is tangible personal property fully exempt from *ad valorem* taxation. The scope of taxation for tangible personal property ranges from all personal property (subject to specified exemptions) to personal property used in business to personal property used by specific types of businesses (*e.g.*, utilities).

The taxation of intangible personal property is more restricted in scope, with only a minority of the states (Alabama, Iowa, Kentucky, Mississippi, Ohio, Pennsylvania, Tennessee, and Texas) subjecting at least some types of intangibles to *ad valorem* taxation. For example, Alabama taxes the franchises and other intangible property of public utilities and the shares of domestic corporations. Florida's annual intangibles tax was repealed, effective January 1, 2007, except as it relates to qualifying government leasehold interests.

General definitions: State definitions of "real property" generally encompass land, any improvements permanently attached to the land, as well as all rights and benefits from ownership of any lifetime or greater interests in such land and improvements. "Personal property" is generally defined by way of exclusion, with all property other than that falling within the definition of real property being considered personal property. The distinction between tangible and intangible property is then commonly made by considering any item of personal property that may be seen, touched, or moved about to be tangible personal property.

Whether a particular item of property constitutes real property or personal property or even tangible property or intangible property is a foundational issue for property tax purposes for a number of reasons. The most significant result of the classification in those jurisdictions that do not generally tax all types of property is that it will resolve the threshold question of whether the property is potentially taxable. For example, in a state such as New York that does not subject personal property to *ad valorem* taxation, characterizing an item as personal property pretty much ends any property tax analysis.

In this regard, the classification issue most frequently arises with respect to machinery or equipment that is attached to or used in conjunction with buildings or other realty. In most states, this problem is addressed statutorily by including "fixtures" within the definition of real property and then relying upon judicial decisions to identify what exactly is a fixture under general real estate law principles. Among the judicial standards used in assessing whether an item of tangible personal property has been converted to a fixture are the following:

— Can the property be removed without damaging the real property to which it is attached?

— Is the property an accessory to the use of the real estate rather than just an accessory to the particular business conducted on the real estate?

— Has the property been physically or constructively annexed to the real property with the intent that it remain annexed indefinitely?

Even in jurisdictions that generally tax both real property and tangible personal property, classification may remain an issue if the assessment ratio or tax rate varies for one type of property but not for the other. In California, for example, the state legislature may either exempt personal property from taxation or provide for differential taxation but may not act similarly with respect to real property.

Classification of property also may affect the tax assessment procedure. For example, depending on the state, the assessment date for real property may be different from that for personal property; the filing of returns (renditions) may be required with respect to personal property but not with respect to real property; and special assessments may be applied only to real property. The classification of property as real property, tangible personal property, or intangible property also may establish which taxing entities have jurisdiction to tax the property, given the different situs rules that may apply.

Significance of situs: Jurisdiction to subject property to *ad valorem* taxation is governed by the concept of "situs." Generally stated, the situs for a particular parcel or item of property is the place where it is legally situated for property tax purposes. For the most part, property is taxable only in those taxing districts within which it is legally situated as of the assessment date.

The situs of real property is where the property is located. The residence or domicile of the owner has no bearing. Given the immovable nature of real property, situs is rarely an issue for such property. When a parcel of real property crosses the boundaries of multiple taxing districts, only the portion lying within each particular district is taxable by that district.

Historically under the doctrine of *mobilia sequuntur personam* (literally, "movables follow the person"), the situs of tangible personal property was considered to be the residence or domicile of the owner. However, most states now treat tangible personal property similarly to real property by identifying the situs as the place where the property is more or less permanently located.

In contrast to the case for tangible personal property, the *mobilia sequuntur personam* doctrine continues to be relied upon in fixing the situs of intangibles by most of the states that subject intangibles to *ad valorem* taxation. Alternatively, a state may provide that the situs is fixed by the business situs of the intangible or by the residence or domicile of the debtor for notes and similar obligations.

Exempt property: State legislatures can, subject to various limits found in the federal Constitution and the applicable state constitution, exempt any persons or property from *ad valorem* taxation or provide comparable tax benefits such as abatements, credits, or reduced assessment ratios. In some cases, the benefit may depend solely on who is the owner (*e.g.,* government, nonprofits and charities, the elderly and disabled, veterans, etc.). However, most frequently the availability of the benefit will be conditioned on the use of the property for a specific purpose. For example, exemptions and/or special tax treatment commonly, but not universally, apply across the states to property use in farming and other agricultural endeavors, property used in manufacturing, pollution control and conservation and "open space" property, inventories, and property temporarily located in the state while in transit out of the state.

Early on in the process, and not uncommonly before the assessment date, property owners must establish their entitlement to any exemption, credit, abatement, or other tax benefit that they expect to claim in connection with their property tax liability and that is not otherwise self executing. Depending upon the benefit, an annual filing may be required to ensure continued entitlement to the benefit, while in other cases a one-time filing may suffice.

- **How is property valued?**

After an assessor has identified all taxable property within the taxing jurisdiction, the property must be "valued" or "appraised." In most cases, the assessor must determine the fair market value of the property, although the states use different terminology to define this standard (*e.g.,* full and true value, actual value, just value, fair cash value, etc.). "Fair market value" is commonly defined as the price in cash for which property would be sold by a willing seller to a willing buyer under normal market conditions, with both parties having full knowledge about the property and neither being under compulsion to buy or sell.

In most cases, property is valued at its objectively determined "highest and best use." However, exceptions to this standard are often provided as a tax benefit to specified types of property (*e.g.,* agricultural land, forest lands, historic property, etc.), which are valued on the basis of their current actual use.

Valuation methods: Assessors typically employ one or more of the following methods in valuing real property:

— the "market data" or "comparable sales" method, under which value is determined by analyzing recent arm's-length sales of similar properties in the vicinity;

— the "cost" method, under which value is determined by analyzing the cost to construct or replace the subject property; and

— the "income" method, under which value is determined by capitalizing the anticipated annual income for the useful life of the subject property.

Although property taxes are levied annually, property is not necessarily assessed or appraised annually. Rather, most states require reappraisals over specified intervals. For example, Illinois generally requires quadrennial assessments (once every four years), while Florida generally requires reassessments every five years.

Personal property generally is valued on the basis of depreciation or "percent good" tables under which an item's value is ratably reduced over its expected useful life. Industry-based valuation guides also are commonly used in valuing personal property.

Returns: The filing of a property tax return, which is also commonly referred to as a "rendition" or statement, is primarily an element of a personal property tax, with taxpayers being required to identify, describe, and give the location of their taxable personal property as of the assessment date. In contrast, annual returns are rarely required for real property tax purposes, given the availability of real property records in most localities. In Texas, for example, taxpayers are not required to file a rendition for other than taxable business personal property, but are instead given the option of filing.

Assessment ratio: Subject to equalization adjustments, in most states a property's fair market value will be the same as its taxable value. However, this will not be the case in states where only a portion of a property's fair market value is taxable. For example, in Connecticut property is taxed at 70% of its assessed value while in Illinois, Indiana, and Iowa, the assessment ratio is generally 33⅓%. In a number of other states, a classified property tax system is employed. In a classified system, property is assigned among designated classes that are differentiated by the use to which the property is put. Each class is then subject to a different assessment ratio (or to a different rate of tax) than the other classes. Examples of common classes are residential, commercial and industrial, agricultural, and utility.

Equalization: Virtually all of the states have a constitutional requirement that assessments be uniform throughout the state. To ensure this requirement is met, most states use a state or local review board to compare the work of local assessors. If inconsistencies are found among jurisdictions or classes of property—which is not an uncommon occurrence given that valuation is far from an exact science—the board can require across-the-board adjustments to be made to correct those inconsistencies.

• **Contesting assessments**

Upon completion of the appraisal of all taxable property within a jurisdiction, the assessor usually is required to notify property owners of the assessed value of their property. Depending upon the jurisdiction, assessors must complete their assessments by a specified date that usually falls within four to six months of the assessment date. The significance of the notice is that it starts the limited time period within which property owners may formally protest the assessed values of their property. In other words, property owners are effectively allowed (or required) to contest their potential tax liability several months before they receive their actual property tax bills.

In most cases, the first appeal of an assessment notice (or denial of an exemption claim) is taken to a local review board, although a few states require property owners to appeal first to their assessor. Usually, the hearings are informal, but do require the filing of a written petition.