



## NEWS YOU CAN USE

### PROPERTY TAX

#### A Texas Challenge

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**T**he City of Austin has found a way to incorporate the slogan “Keep Austin Weird” into Travis County’s property tax system by challenging the 2015 commercial tax roll. Specifically, the city challenged Travis County Appraisal District’s (TCAD) valuations for the categories of F1 Commercial Real Properties (office, retail and industrial) and C1 Vacant Lots (commercial vacant land). Interestingly, the challenge excluded category B, multi-family residences, which makes up a sizable component of the commercial tax roll.

In Texas, a taxing unit may challenge the level of appraisals of any category of property within the district before the appraisal review board (ARB).<sup>1</sup> In May, the City of Austin filed a petition challenging the appraisal records claiming that the initial appraised values for commercial property in 2015 were undervalued by 40%.<sup>2</sup> The city’s challenge was spurred by the results of a report it commissioned, which concluded that the TCAD had undervalued improved and unimproved commercial property by an average of 47% from 2012 through 2014.<sup>3</sup> In fact, the city considered filing a challenge in 2014; however, they opted instead to commission this report in preparation for the 2015 challenge.

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The report was conducted by The Aegis Group for \$380,000 and was based on 429 sales transactions that occurred between 2012 and 2015. The report purports to adjust the sales for differences in time and above market leasehold interests. Further, the report claims to exclude non-arm’s length transactions, properties with significant business value, and tax-exempt properties from the analysis. In response to the report, Marya Crigler, the TCAD Chief Appraiser, stated that “it became apparent that several items in the statistical analysis were vague, potentially misrepresented and painted a picture that wasn’t what was being described by the council.”<sup>4</sup>

Austin’s challenge is an outgrowth of the notion that residential taxpayers are burdened with a disproportionate tax liability when compared to commercial taxpayers. This ideology gained momentum in the fall of 2014 when Houston media outlets asserted that residential properties were systematically being assessed at market value whereas commercial properties were routinely assessed for much less. Real Values for Texas, a new group with membership that includes AFL-CIO Houston, Service Employees International Union and MoveOn.org, circulated this storyline. These media outlets maintained that commercial property owners achieved tax breaks by using a “loophole” in the current tax law to secure low appraised values. Additionally, they averred that appraisal districts are at a disadvantage in appraising commercial properties, as opposed to single-family residences, because Texas is a non-disclosure state and commercial sales data can be difficult to obtain. Such a challenge

is premised on the notion that recouping commercial property owner tax dollars would lead to an increase in goods and services provided by counties, cities and school districts, and a decrease in the tax rates imposed by taxing jurisdictions.

The publicity of perceived “loopholes” in the property tax system and lack of sales disclosure brought about the first tax roll challenge, which occurred in Harris County in June of 2014. Interestingly, the former chief appraiser of the Harris County Appraisal District (HCAD), Jim Robinson, was instrumental in the 2014 Harris County challenge. Mr. Robinson retired from HCAD in May of 2013 and spent 23 years at HCAD developing its methodology and standards. However, within a year of his retirement he and others were convinced that HCAD was undervaluing commercial property.

<sup>1</sup> Tex. Tax Code Ann. § 6.01(b).

<sup>2</sup> Austin American Statesman, June 2, 2015.

<sup>3</sup> George W. Gau, Ph.D. and Robert S. Radebaugh, MAI (2015). *An Analysis of TCAD’s Commercial Valuations For City of Austin*.

<sup>4</sup> Austin Chronicle, June 12, 2015.

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Consequently, the Harris County Commissioners' Court commissioned a study by Ted Whitmer, an MAI and CCIM, to perform an analysis testing the accuracy of HCAD's appraisals. The Whitmer Study claimed that HCAD undervalued vacant land by more than 80% based on 2014 preliminary values. However, the study further found that HCAD accurately appraised all other classes of commercial property. Therefore, in July of 2014 the Commissioner's Court withdrew their challenge after agreement was reached to "share information moving forward." One can only speculate as to why Harris County dropped its challenge, however; it is important to note that the Texas Comptroller's Property Valuation Study certified that HCAD had valued commercial properties properly within acceptable ranges. Further, HCAD retained the property taxation and consultant firm of Almy, Gloudenmans, Jacobs and Denne to independently evaluate the accuracy of HCAD's tax roll. The results of HCAD's study showed that HCAD's appraisals were sufficient, thus there was no challenge in 2015.

In June 2014, the Travis County Commissioners Court formed a citizen task force to look into the issue. Contrary to the City of Austin's actions, the Commoner's Court eventually voted down a proposal to challenge TCAD for tax years 2014 and 2015.

Clearly the City of Austin recognized that its unprecedented challenge before the ARB would cause a delay in the issuance of tax statements and the collection of property taxes in 2015. Thus, city and TCAD attorneys asked the Travis ARB to deny the city's petition. This joint action relieved the concerns of other local taxing entities that feared a delay in tax roll certification and cleared the way for an appeal directly to district court. Mayor Steve Adler stated that the "city legal staff will move their challenge from the Appraisal Review Board to a district court, thereby avoiding a delay in the certification of the tax roll, which could have rippled through the budget processes of the county's 100-odd taxing entities."<sup>5</sup>

Many questions are raised by these Harris County and City of Austin challenges. First, let's discuss the alleged "loophole" tax law, the Remedy for Unequal Appraisal.<sup>6</sup> This was a piece of legislation passed by the Texas Legislature and signed by the Governor in 1997. The unequal appraisal remedy provides that "the district court shall grant relief on the ground that a property is appraised unequally if the appraised value of the property exceeds the median appraised value of a reasonable number of comparable properties appropriately adjusted."<sup>7</sup>

Appraisal districts and local governments have fought this law in the Texas Legislature since its inception. At issue is the long-held principle that similar properties should be appraised at similar values in order to ensure equal treatment among taxpayers. Historically, the remedy for unequal appraisal has protected taxpayers against unfair treatment by appraisal districts as taxpayers could rely on the "equal and uniform" argument on appeal. Indeed, this principle is enshrined in the Texas Constitution.

The courts have consistently upheld § 42.26(a)(3) of the remedy for unequal appraisal since it was initially challenged in 2001 in *Harris County Appraisal District v. United Investors Realty Trust*. In *United Investors*, the court held that "if a conflict exists between taxation at market value and equal and uniform taxation, equal and uniform taxation must prevail."

Another question raised by these challenges is whether single-family residential property owners are actually shouldering more than their fair share of the property tax burden. There are numerous factors that counter this assertion:

- The Texas Taxpayers and Research Association states that 63.5 percent of all state and local taxes are paid by Texas businesses.
- The Comptroller's 2014 Property Valuation Study states that business taxpayers pay the majority of all property taxes in Texas.
- The Comptroller's Biennial Property Tax Report states that between 2012 and 2013 commercial property valuations increased an average of 8.48 percent statewide, twice the rate of single-family residential properties.
- Approximately 70 percent of all Texas exemptions apply exclusively to single-family residential properties.
- Homesteaded single-family properties valuations are capped and cannot raise more than 10 percent each year.

By making these challenges, both Harris County and the City of Austin are emphatically stating that they have no confidence in the Texas Comptroller's Property Valuation Studies. These studies serve as an oversight function by the state to test the accuracy of appraisal district valuations. The State of Texas and local governments depend on these studies and undermining them is a negative for the Texas property tax system.

Critics further argue that mandatory sales disclosure should be required in Texas to assist appraisal districts in valuing commercial properties. While Texas is a non-

<sup>5</sup> Austin Monitor, June 19, 2015.

<sup>6</sup> Tex. Tax Code Ann. § 42.26(a).

<sup>7</sup> Tex. Tax Code Ann. § 42.26(a)(3).



disclosure state, appraisal districts do have access to data sources such as Costar, LoopNet and other sources made available to the public. Further, closing statements are routinely turned over to appraisal districts during the appeal process. The political reality is that sales disclosure legislation fails every session as the powerful real estate community opposes it for multiple reasons, such as a potential transactional tax.

Since the remedy for unequal appraisal (§ 42.26(a)(3)) and sales disclosure are perceived as major issues, both were attacked during the 2015 legislative session. Lines were drawn and coalitions were formed both supporting and opposing the existing laws. Opposing to the current tax laws were local governments, appraisal districts and a group called Real Values for Texas. Supporting the current law was the Texas Association of Property Tax Professionals and the newly formed Coalition for Equal and Uniform Taxation. This politically influential group included every major association of commercial property owners and managers within Texas.

By the end of the 2015 Session, House Bill 2083 passed and was signed by the Governor. This bill added new language affecting the remedy for unequal appraisal. Specifically, the selection of and adjustments to comparable properties in a § 42.26(a)(3) appeal must now be based on the application of generally accepted appraisal methods and techniques.<sup>8</sup> Further, property owners representing themselves are entitled to offer opinion and present argument and evidence related to the market value or inequality of their property.<sup>9</sup> Some argue that the new language is benign and others think only future court rulings will define what the verbiage means in a legal sense.

The Texas Property Tax Code states that property, unless otherwise exempt, shall be appraised at its market value as of January 1 of each tax year.<sup>10</sup> The Code goes on to state that taxpayers have the right challenge unequal appraisals.<sup>11</sup> Clearly the City of Austin is attempting to secure its interpretation of market value for certain segments of its 2015 tax roll. Through the city's action of including some segments in the challenge while excluding others, it appears to ignore the Texas Constitutional provision that taxation should be equal and uniform.

The City of Austin's challenge is unprecedented and if successful it would bring chaos and a whirlwind of uncertainty in its property tax system. For example, if TCAD were forced to reappraise commercial properties and vacant land, what effect would it have on taxpayers who have already appealed their property through the administrative remedy level? Taxpayers who have reached settlements or received ARB determinations should not be forced to endure the appeal process for a second time and face the possibility of a drastic increase in their tax liability. This is especially true for property owners who undertake the extra costs of litigation and obtain relief through district court.

In reality, the City of Austin's challenge has the potential to hold the property tax system at ransom—threatening massive governmental expenditures and years of litigation in the hope of gaining lower tax rates for residential homeowners and renters. The constitutional mandate that taxation be equal and uniform applies to all property owners in the state of Texas; however, the City of Austin's

challenge has singled out only segments of the property tax roll without evaluating others. The city's challenge is a direct attack against the Comptroller's Property Valuation Studies, which have consistently shown that Travis Central Appraisal District has adequately

appraised commercial property. The only thing that is certain following the City of Austin's challenge is the city's adherence to its slogan "Keep Austin Weird."

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<sup>8</sup> Tex. Tax Code Ann. § 23.01(f).

<sup>9</sup> Tex. Tax Code Ann. § 23.01(g).

<sup>10</sup> Tex. Tax Code Ann. § 23.01(a).

<sup>11</sup> Tex. Tax Code Ann. §§ 41.41(a)(2) and 42.26(a)(1-3).