

State Tax Commission



Guide to Basic Assessing

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Chapter 1

History of Property Tax, Local Government Finance and Property Taxation

Local governments receive revenue from a variety of sources including property taxes, permit fees, user charges (recreation programs, water bills), and voted debt millages. Local governments also receive funding from the federal government in the form of grants and from state government in the form of revenue sharing and grants. Property taxes are the largest revenue stream for local government.

Michigan's property tax has been a territorial tax since it was authorized by the Northwest Land Ordinance of 1787. All property, real and personal, was taxed until the 1940s when personal property was eliminated for individual households but retained for commercial and industrial businesses.

Michigan became a state in 1837 and a Constitution was adopted. The first revision to the Constitution was in 1850 when a provision was added providing for a uniform rate of taxation as well as the continuation of existing taxes and the use of true cash value assessments. The County sheriff collected the taxes and that is probably why the County sheriff holds the delinquent tax sales to this day.

In 1850, only the counties, Townships, and school districts were allowed to levy taxes. Today, counties, cities, Townships, school districts, intermediate schools, community colleges, libraries, airport, transportation, and other agencies may levy taxes. In 1994, the state returned to the property tax business with the passage of Proposal A.

In 1909, the Home Rule City Act was approved, which allows cities to determine the type of government they wish to form through City charter, to establish their own tax rate and to collect property tax through the City Treasurer.

Townships are still the most basic form of government in Michigan. If the population of a Township exceeds 2,000, they may become a Charter Township.

The Michigan General Property Tax Act

The Michigan General Property Tax Act, Public Act 206, was enacted in 1893. It states that "all property, real and personal, within the jurisdiction of this state, not expressly exempted, shall be subject to taxation."

Exemptions were continued for the U.S. government, state and local governments, religious, charitable, and educational organizations. Exemptions were included for a variety of nonprofit organizations as well as basic exemptions for household goods, tools, and agricultural property. Public utilities, railroads, and telephone and telegraph properties as well as intangibles were taxed by the state. Through the years exemptions were added for special tools such as dies and jigs to encourage

manufacturing. In the 1970s, exemptions were established for businesses that created or expanded their business in Michigan.

The procedures and schedules established by the General Property Tax Act that are still followed today are as follows:

1. Local preparation and review of the assessment roll.
2. County and state review of assessment rolls to equalize true cash values used for assessments.
3. Certification of taxes to local unit and to County Board of Commissioners.
4. County Board of Commissioners review tax levies, apportions the tax, and authorizes spread of taxes by local unit.
5. Preparation of tax rolls and delivery to the treasurer.
6. Disbursement of taxes to local units.
7. Collection of delinquent taxes by the County treasurer and execution of tax liens.

Equalization departments in Michigan were established in 1909 to avoid owners of similarly valued properties from paying different amounts of state property taxes. County Equalization takes place in April and State Equalization, a function of the State Tax Commission, is in May of each year.

Tax Reform

In Michigan, the earliest tax reform took place in 1932 when the Constitution was amended. The amendment included a provision that the basic tax rates allowed to be levied by local government without a vote of its citizens is limited to an amount that would not generate tax revenue that exceeded 1½% of the assessed value of the property being taxed. Several amendments have been made to this limit and to the 15-mill limit allowed by the Constitution.

In 1934, the state implemented a sales tax and left the property tax for local government to split. In 1948, the constitution was amended to permit levying an additional tax for up to 20 years for a specific purpose. A 1955 amendment excludes from the limitation taxes used for paying certain types of school bonds.

The 1963 Michigan Constitution continued this limitation on total tax rates. It does not however, provide for allocation of the 15 mills (or 18 mills) among local government units. The voters of most counties have approved a fixed millage allocation for the County. For the counties that do not have a fixed millage allocation, there is a County allocation board that allocates the 15 mills. Tax allocation begins on the third Monday in April. Each unit submits a budget for the board's review.

The allocation board may not allocate the entire 15 mills because the Property Tax Limitation Act guarantees the following minimum rates:

County	3 mills
Township	1 mill
Intermediate School District	.1 mill
Community College	.25 mill
School District	4 mills (prior to Proposal A)

Today, due to Proposal A, the school district does not receive the 4 mills. The state gets 6 mills for education.

On the third Monday in May, the allocation board issues a notice of preliminary tax allocation along with the time of a public hearing. Any taxing authority may be heard at the public hearing.

Most governmental units levy taxes well beyond the 15/18 allocated millages. These millages can be:

1. Voted millages for operating or building.
2. Millages contained in the charter.
3. Millages used for repayment of bonds.

There is no limit on taxes imposed for repayments of principal and interest on voter-approved bonds. There are limits on the amount of debt a taxing unit can incur. Charter counties, charter Townships, and charter and general villages may incur bonded indebtedness up to 10% of their state equalized value. The authority of general law Townships is much more severely restricted.

Headlee Tax Limitation

In 1978, the voters approved what is known as the Headlee Amendment. The amendment is important because it was the first successful amendment to the 1963 Constitution that limited taxes. The provisions of Headlee that affect local government are as follows:

1. The state must maintain the same proportion of spending paid to local government as was paid in 1978.
2. Prohibit the state from imposing new mandates on local government unless the state funded such programs.
3. Prohibit local units from imposing new taxes, raising existing taxes, or bonding general obligation debt without the voter's approval.

4. Limited local tax revenue growth by requiring reduction of maximum authorized tax rates to offset growth in assessed values that exceed the general price level of the previous year. This is accomplished by applying a millage rollback fraction.

The formula for this millage rollback fraction (MRF) is:

$$\frac{(\text{Prior Year Total Taxable Value} - \text{Losses} \times \text{IRM})}{\text{Current Year Taxable Values} - \text{Additions}} = \text{Current Year MRF}$$

This fraction is calculated each year and adjusted for inflation. It is applied to the prior year's maximum allowable millage rate (MMRA).

Truth in Taxation was passed in 1982. Its purpose was to require public notice and a public hearing before it a vote can take place on a millage increase up to the Headlee limit.

Proposal A

In July of 1993, the legislature voted to eliminate property taxes as the source of school funding because of increasing reliance on property taxes for K-12 funding and the wide variation of per pupil spending between districts.

In March of 1994, the voters approved Proposal A which replaced most of the school property taxes with an increase in the sales tax. This was the first statewide tax proposal in 20 years to be successful.

The primary components of Proposal A are as follows:

1. School property taxes in all districts were reduced to 18 mills or the number of mills levied in 1993 for school operating.
2. Homestead property and qualified agricultural property are exempt from the 18 mills.
3. A new value known as the "taxable value" was created. Each parcel now has three values, a capped value, an assessed value (SEV) and a taxable value. For tax purposes, the taxable values were capped at the 1994 value and can only increase at the rate of inflation or 5%, whichever is less. When a property sells it is uncapped and the state equalized value and the taxable value are the same for the next year. It is then recapped until it sells again.
4. Sales tax was increased from 4 to 6 cents per dollar. A statewide 6-mill State Education Tax was levied on all property. Taxes were increased on alcohol and tobacco and for the real estate transfer tax.
5. The constitution was amended to exempt school taxes from the uniformity provision of the constitution and any increase in school operating taxes now requires a $\frac{3}{4}$ vote of both houses of the legislature.

6. Each school district receives a per pupil allotment from the state that is funded by the increase in sales and other taxes.

The results of Proposal A were immediate. Property taxes went down dramatically for homesteaded property and to a lesser degree for non-homestead properties. Per pupil spending increased in many school districts. Property taxes were held at a lower rate even in the face of increasing property values.

The long term effects of Proposal A are now being felt in local units throughout the State as property values have declined dramatically over the past 3 years and for the first time ever, the State had a negative inflation rate multiplier for the 2010 year.

Business Property Tax and Economic Development

Various Property tax relief is available that can be used by businesses. Some are included as follows:

1. Assessment challenges to the assessed values of businesses – both real and personal – through the local Board of Review and Michigan Tax Tribunal.
2. Tax abatements in the form of reduced millage rates for businesses that make a significant investment in either new or rehabilitated buildings and new equipment and machinery. P. A. 198 of 1974, Industrial Facilities Tax exemption.
3. P.A. 328 of 1998, also known as the New Personal Property exemption.
4. P.A. 451 of 1994, Air & Water Pollution Control exemption.
5. P.A. 210 of 2005, Commercial Rehabilitation exemption

Exemptions reduce the property tax burden of a taxpayer for every year in which they are granted. Abatements either, preserve the tax base or increase the tax base, while providing a reduced future tax burden on new investments. Tax Capturing Authorities do not affect the tax base at all; they affect the distribution of taxes.

In December of 2012, initial legislation was passed that significantly changed the taxation of personal property. The Acts exempt personal property from taxation through two main provisions: Small Business Taxpayer Exemption (MCL 211.9o) and Eligible Manufacturing Personal Property Exemption (MCL 211.9m and MCL 211.9n). The Acts also identified a specific replacement tax on personal property (Essential Services Assessment) and reimbursement for local unit's lost revenue. These exemptions are detailed in a later Chapter.

Administration of Property Tax Law

Property Tax Law is adopted and amended by the legislature. The administration of the law is performed at the local level. The State Tax Commission has general supervision of the administration of the tax laws of the State, and is statutorily required to "render" assistance and give advice and counsel to the assessing officers of the state as they

may deem necessary and essential to the proper administration of the laws governing assessments and the levying of taxes in this State. Executive Order 2009-51, which took effect on December 28, 2009, gave the State Tax Commission authority over all aspects of the general property tax, including the certification and education of assessors.

Chapter 2 Property Tax Law, the Tax Calendar, Exemptions and Abatements

Note: All STC publications including bulletins, letters, guidelines and Q and A's are available on the STC website at www.michigan.gov/statetaxcommission.

The authority of government to levy taxes is contained in Article 9 of the Constitution of the State of Michigan. Article 9, Section 3, states that all property shall be assessed uniformly and shall not exceed 50% of true cash value.

The Michigan Constitution provides for exemption of real and personal property owned and occupied by nonprofit, religious, and educational organizations. It also requires that increases to the ad valorem tax must be submitted to the electors for a vote before the tax may be levied.

Section 25 of Article 9 prohibits the state from requiring new or expanded activities to be provided by local government unless the state provides the funding for those activities.

The General Property Tax Act, Public Act 206 of 1893, is the usual reference source regarding the assessment and taxation of real and personal property.

Section 211.1 Property subject to taxation: All property in the state, both real and personal, is taxable unless specifically exempted.
211.2...211.6b Real Property.
211.7...211.7nn Real Estate Exemptions.
211.8...211.8c Personal Property. Personal property is assessed to the owner and is assessed by the unit where it is located on December 31 (SITUS). Personal property tax bills are based on the personal property statement submitted by the business owner or agent on or before February 20 of each year. Failure to submit a personal property statement will result in the assessor setting an assessment he/she believes is fair and just.
211.9...211.9o Personal Property Exemptions.
211.10...211.17 Assessments. Section 211.10d addresses the certification of assessors. For a newly elected Township Supervisor in a community requiring a Michigan Certified Assessing Officer, a 6-month conditional certification may be granted. If a unit does not have a qualified assessor, the assessments are made by the County Equalization department and the cost of preparing the roll is charged to the local assessing unit. It is a misdemeanor to certify a roll that you have not prepared or supervised. If a unit does not have a properly certified assessor, the State Tax Commission shall assume jurisdiction of the assessment roll and provide a certified roll. Costs are paid by the local unit.
Section 211.14(6) states that after December 31, 2002, buildings and improvements on leased lands shall be assessed as real property. Sections 211.10 through 211.23 address

assessments and how they are to be made and by whom (certified assessor using STC approved manual). If a real or personal property is not specifically exempted by the act, it is not exempt.

Assessments are made on an annual basis and are determined on December 31, tax day. Assessments for a village and the assessments of the Township in which it is located are made by the same assessor. If the assessor changes the assessment on a property, he/she must notify the owner of the property not less than fourteen days prior to the meeting of the Board of Review of the new assessed value. If a property owner wishes to review his/her assessment records, the assessor should make every effort to accommodate the taxpayer during normal business hours. Failure to receive a notice of assessment change does not invalidate the assessment. All assessment rolls must be completed and turned over to the Board of Review on the Tuesday following the first Monday in March.

211.18...211.23a Assessment, How to Make.

211.24...211.27d Assessment Roll.

211.28...211.33 Board Of Review. The Board of Review (BOR) consists of 3, 6, or 9 electors of the local unit. The Board of Review is appointed by the council, commission, or board for two years. Elected officials and relatives of the assessor are prohibited from serving on the board. BOR meetings on the first two days must be six hours and one of the meetings must be held after 6:00 p.m. In a Township, the Supervisor is the secretary of the BOR or he/she may appoint someone to act as secretary. The BOR hears petitions from taxpayers or their agents regarding assessments and may also hear appeals of classification. Poverty appeals may be heard at the March, July, or December Board of Review. Appeals may be made in person or by mail.

The Board may reduce or raise an assessment on their own motion. Decisions of the Board may be appealed to the Michigan Tax Tribunal (MTT) and not to the STC with the exception of classification appeals. Notices of the decisions of the Board must be mailed by June 1.

The Board of Review is also authorized to hold two meetings (July and December) to correct mutual mistakes of fact, clerical errors or qualified errors. The Board may also hear homestead appeals.

211.34...211.34e Equalization By Counties. Section 211.34c defines property classification. Real property is classified as: *Agricultural, Commercial, Developmental, Industrial, Residential, and Timber-Cutover*. Parcels used for recreational purposes are classed *Residential*. Personal property is classified as: *Agricultural, Commercial, Industrial, Residential, and Utility*. Farm buildings on leased land would be an example of agricultural real property.

211.35...211.38 Taxes, Certified how and by Whom.

211.39...211.41a Taxes—How To Be Assessed. Sections 211.39 through 211.144 deal with taxes and how they are spread, how they are collected and delinquent taxes and how delinquent properties are handled. Taxes are spread on **taxable value** since the passage of Proposal A. Taxes are a lien on the property. Local units may add a 1% administration fee to the property taxes collected. Taxes are due by February 14 and if not paid by that date interest begins to accrue. Local treasurers collect taxes until March 1. At that time the taxes are turned over to the County treasurers as delinquent. After March 1, taxes must be paid to the County treasurer.

211.42...211.43c Tax Roll.
211.44...211.54 Collecting Of Taxes.
211.55...211.59 Return Of Delinquent Taxes.
211.60...211.60a Sale, Redemption And Conveyance Of Delinquent Tax Lands.
211.61...211.69 Notice And Lists Of Lands To Be Sold.
211.70...211.73c Sale By County Treasurer.
211.74...211.79a Redemption And Annulment.
211.83...211.86 Tax Lands Held By The State.
211.87...211.91 Accounts And Settlement Thereof.
211.92...211.126 Miscellaneous Provisions.
211.127b...211.134 Inspection And Disposition Of State Tax Lands.
211.135...211.157 and 209.101 through 209.107. Sections 211.146 through 211.154 as well as 209.101 through 209.107 outline the duties and responsibilities of the State Tax Commission. The State Tax Commission members are appointed by the Governor. The STC is subject to the Open Meetings Act and to the Freedom of Information Act. They are required to meet six times a year. Their duty is to supervise assessors and ensure that all property in the state subject to taxation are assessed and taxed according to statute. They also certify personal property examiners (PPE). They investigate all complaints related to fraudulently or improperly assessed properties and have the authority to correct erroneous assessments due to incorrect reporting or omitted reporting of property and to order additional tax billing or refunds.

The most recent Property Tax Calendar can be found on the State Tax Commission's Web Site at www.michigan.gov/statetaxcommission.

Exemption Programs:

In Michigan, two guiding principles have developed to address taxation in general, and exemptions, from the ad valorem tax: (1) "In general, tax laws are construed against the government;" and (2) tax exemption statutes are strictly construed in favor of the government.

The mechanism of an exemption is simple: it reduces a property's tax obligation and provides immediate property tax relief. Unlike exemptions, abatements reduce the maximum future tax burden on investments by a taxpayer. Abatements modify either the millage rate or taxable value used to calculate taxes if, an investor improves either real or personal property.

Air Pollution Control: P.A. 451 of 1994, Part 59

The Air Pollution Control exemption provides a 100% property and sales tax exemption to facilities that are designed and operated primarily for the purpose of controlling or

disposing of air pollution that, if released, would render the air harmful or inimical to the public health or property within this state. The STC is responsible for final approval and issuance of air pollution control certificates. Exemptions are not effective until approved by the STC.

This law provides a 100% exemption from property taxes that would be levied on otherwise taxable property. The exemption is granted on property defined as a “facility” in MCL 324.5901(a), (b) or (c).

Water Pollution Control: P.A. 451 of 1994, Part 37

The Water Pollution Control exemption affords a 100% property and sales tax exemption to facilities that are designed and operated primarily for the control, capture and removal of industrial waste from water. The exemption applies to property not previously certified as pollution control; even if the property is currently assessed on the ad valorem roll.

The STC is responsible for final approval and issuance of water pollution control certificates. Exemptions are not effective until approved by the STC.

This law provides a 100% exemption from property taxes that would be levied on otherwise taxable property. The exemption is granted on property defined as a “facility” in MCL 324.3701(a), (b), (c) or (d).

New Personal Property Exemption: P.A. 328 of 1998

This exemption provides a 100% property tax exemption for all new personal property owned or leased by an eligible business located in one or more eligible districts or distressed parcels within an eligible local assessing district. The district or the eligible distressed area has to be established prior to an application for an exemption certificate. The exemption applies to all new personal property, not previously subject to tax under the GPTA and placed in a district after the adoption of a resolution approving the application by the governing body of the eligible local assessing district.

This exemption applies to new personal property of a business engaged primarily in manufacturing, mining, research and development, wholesale trade or office operations. Property within an “authorized business” as defined in Section 3 of the Michigan Economic Growth Authority Act (MEGA) is eligible for credits described in Section 9 of the MEGA act. The benefit is not extended to: a casino, retail establishments, professional sports stadium or that portion of an eligible business used for retail sales.

Disabled Veterans Exemption: MCL 211.7b

Real property used and owned as a homestead by a disabled veteran who was honorably discharged from the armed forces is exempt from property taxes under the General Property Tax Act. This exemption is also extended to the unremarried surviving

spouse of the disable veteran, provided that the disabled veteran qualified for the exemption prior to their death.

In order to qualify for the exemption, the disabled veteran must live in the home and own the home (i.e. their name must be on the deed to the home). The State Tax Commission has determined that the home must be in the name of the disabled veteran and their spouse only and there cannot be any other ownership interest in the home. The Act defines a disabled veteran as a resident of the State of Michigan who meets one of the following criteria:

- (a) Has been determined by the United States department of veteran's affairs to be permanently and totally disabled as a result of military service and entitled to veterans' benefits at the 100% rate.
- (b) Has a certificate from the United States veterans' administration, or its successors, certifying that he or she is receiving or has received pecuniary assistance due to disability for specially adapted housing.
- (c) Has been rated by the United States department of veteran's affairs as individually unemployable.

More detailed information can be found on the STC website the Disabled Veterans Exemption link.

Principal Residence Exemption (PRE): MCL 211.7cc

A principal residence is exempt from the tax levied by a local school district for school operating purposes up to 18 mills if an owner of that principal residence claims an exemption as provided in MCL 211.7cc. A person must own and occupy the property as his or her principal residence on or before June 1st to claim the exemption for the summer tax levy or November 1st for the winter tax levy. The June 1 and November 1 dates also apply to Conditional Rescissions and Foreclosure Entity Conditional Rescissions.

To claim a PRE, the owner must file a Principal Residence Exemption Affidavit, Form 2368, (Affidavit) with the assessor for the City or Township in which the property is located. The Affidavit is a sworn statement attesting that they are an owner that occupies the property as his or her principal residence. Normally, when a home is purchased, the Affidavit and other relevant PRE forms are provided by the closing agents. If the assessor believes an Affidavit is not valid, they should deny the claim and provide the taxpayer with their appeal rights. As with any tax exemption, the burden is on the taxpayer to show that they are entitled to a PRE.

Public Acts 121 and 122 of 2017 amended MCL 211.7cc and MCL 211.120 to provide that the assessor of a local tax collecting unit, the Department of Treasury, or a county treasurer or equalization director can require a person within 30 days of claiming the PRE, to file the Principal Residence Exemption Affidavit of Similar Exemption in Other

States, Form 5565, stating that he or she had not claimed a substantially similar exemption, deduction, or credit in another state.

Public Act 121 also prohibits a person from rescinding a substantially similar exemption, deduction, or credit claimed in another state in order to qualify for the Michigan PRE for any years denied, if the assessor of a local tax collecting unit, the Department of Treasury, or a county denied an existing claim for a PRE. The Act also prescribes a penalty of \$500 for a person who claimed a PRE under the Act and a substantially similar exemption, deduction, or credit in another state.

Public Act 122 amends the General Property Tax Act to extend a misdemeanor penalty to a person who claimed a substantially similar exemption, deduction, or credit on property in another state with the intent to obtain a PRE under the Act.

When an Affidavit is filed, it is important to verify that the person submitting the Affidavit meets the definitions of an “owner.” MCL 211.7dd(a) defines an “owner” as:

- A person who owns property or who is purchasing property under a land contract.
- A person who is a partial owner of property.
- A person who owns property as a result of being the beneficiary of a will, trust or intestate succession. (The beneficiary is considered the owner for PRE purposes upon the death of the grantor).
- A person who owns or is purchasing a dwelling on leased land.
- A person holding a life lease in property previously sold or transferred to another. (The life lease holder must have been a previous owner).
- A grantor who has placed property in a revocable trust or a qualified personal residence trust. (A qualified personal residence trust may be irrevocable. All other irrevocable trusts do not qualify).
- The sole present beneficiary of a trust if the trust purchased or acquired the property for a beneficiary who is totally and permanently disabled.
- A cooperative housing corporation.
- A facility registered under the Living Care Disclosure Act.

It is important to note that a “person” as used in the above definitions means an individual and does not include a partnership, corporation, limited liability company, association, or other legal entity. The percentage of ownership a person has in property is generally not relevant as long as that person meets the definition of an owner and occupies that property as a principal residence. In other words, a person that is a 1% owner of a property and occupies that entire property as a principal residence may qualify for a 100% PRE.

The following factors must also be considered when evaluating an owner's eligibility for a PRE:

- A husband and wife who file, or are required to file, a joint Michigan income tax return are entitled to not more than one PRE.
- If a person claims a substantially similar exemption in another state which has not been rescinded, they do not qualify for a PRE in Michigan.
- If a person files an income tax return as a resident of another state, (active military personnel excluded), they do not qualify for a PRE in Michigan.
- If a person files a non-resident Michigan income tax return, (active military personnel with his or her principal residence in this state excluded), they do not qualify for a PRE in Michigan.
- If a person or his or her spouse owns property in another state for which either person claims an exemption similar to the PRE, they do not qualify for a PRE in Michigan, unless they file separate income tax returns.

What is a Principal Residence?

MCL 211.7dd(c) defines a principal residence as the "... [one] place where an owner of the property has his or her true, fixed, and permanent home to which, whenever absent, they intend to return and that shall continue as a principal residence until another principal residence is established." Although this is not an all inclusive list and no one factor is controlling, the following is a list of items to consider:

- Location of a person's most important possessions.
- Where the family is housed.
- Voting location.
- Where church, club and lodge memberships are maintained.
- Where a person buys automobile licenses.
- Mailing address and banking location.
- Operation of a business.

A principal residence also includes the owner's unoccupied property classified as residential or timber-cutover that is adjoining or contiguous to the dwelling owned and occupied by the owner. The property is generally considered unoccupied if it does not contain a habitable dwelling. Properties containing a garage, storage building and other similar structures normally are considered unoccupied unless they contain living quarters. Contiguity is not broken by a road or a right-of-way. An adjoining or contiguous property classified as agricultural, developmental, industrial or commercial does not qualify for a PRE.

Determining Eligibility for PRE:

Determining whether a person occupies a property as a principal residence can be very challenging. Generally, a person must physically occupy or live at the property by June 1st for the summer tax levy or November 1st for the winter tax levy of the year they are claiming the PRE. There are a number of ways to verify occupancy. The following occupancy verification list is not an all inclusive list and no one factor is controlling:

- Both sides of a driver's license with the property address listed.
- Voter's registration record.
- Cancelled checks showing the property address.
- Bank/charge accounts showing purchases within the vicinity of the property.
- Medical billings from physicians within the vicinity of the property.
- Income tax returns showing the mailing address.
- Insurance policies.

Because of the definition of a principal residence, temporary absences are allowed in some circumstances which can make verifying occupancy even more difficult. Some examples of temporary absences include: prisoners with a less-than-life sentence, a person in a nursing home or assisted living facility, missionaries, a person on an extended work assignment, a person renting an apartment while renovating a home, or military personnel. With any temporary absence, the owner must have the intent to return to the property to again occupy it as a principal residence.

Determining this "intent to return" can be very difficult. If a person changes a driver's license address or registers to vote at a new location, his or her intent to return to the property may be in question. If the property is rented or is listed for sale, a reasonable person may conclude that there is no intent to return to the property. When an owner's personal possessions are removed from the property, it is hard to argue that they intend to return to that property. The length of absence or the reason for the absence may also raise questions as to the owner's intent to return to the property. Ultimately, the burden is on the taxpayer to show that they are eligible for the PRE.

Partial PRE Exemptions:

If a property is used for multiple purposes, only the percentage of the property occupied by the owner as a principal residence may qualify for a PRE. When a person operates a business out of the property, rents a portion of the home to a tenant or owns multi-dwellings such as duplexes, the owner may be eligible to claim a portion of the property occupied as the owner's principal residence (MCL 211.7cc(16)). If the property contains one building, the PRE is reduced by the proportion of the square footage not used as the owner's principal residence. If the property contains two or more buildings, the PRE

is reduced by the proportion of the taxable value/assessed value of the building not used as the owner's principal residence.

For owners who rent a portion of their home to a tenant, the owner is entitled to a 100% PRE if less than 50% of the square footage is rented (MCL 211.7dd(c)). If an owner rents his entire property for more than 14 days in a year, they are not entitled to a PRE on that property (IRS Publication 527, Chapter 5, Page 21). A portion of a bed and breakfast may also qualify as a principal residence, MCL 211.7cc(28).

Military Personnel Considerations:

Military personnel are given special consideration when evaluating principal residence. When military personnel are required to leave Michigan while on active duty, they may continue to qualify for a PRE in Michigan. In order to qualify, they must be an owner of the property as defined by MCL 211.7dd. In addition, they must have occupied the property as a principal residence prior to deployment and have the intent to return to the property after the active duty commitment is complete. In order to continue to receive the PRE in Michigan, military personnel cannot receive an exemption, deduction or credit similar to the Michigan PRE in another state. If someone wishes to rent out his or her property during an absence while on active duty military, they may file an Active Duty Military Affidavit, Form 4660, on or before May 1st with the local assessor where the property is located.

Rescinding a PRE Exemption:

When a person no longer owns or occupies the property as a principal residence, they must file a Request to Rescind Homeowner's Principal Residence Exemption (PRE), Form 2602, (Rescission) with the assessor for the City or Township in which the property is located to remove the PRE. The PRE will be removed from the local property tax roll by the assessor beginning with the next tax year.

A PRE on a foreclosed property should be removed on December 31st in the year of the foreclosure or Sheriff's sale. If the property is redeemed, the PRE may be reinstated upon filing of the Affidavit and, if needed, brought before the Board of Review so there is no break in the exemption.

Under certain circumstances a person may qualify for a **conditional rescission** which allows an owner to receive a PRE on his or her current Michigan property and on previously exempted property simultaneously for up to three years. To initially qualify for a conditional rescission, the owner must submit a Conditional Rescission of Principal Residence Exemption, Form 4640, to the assessor for the City or Township in which the property is located on or before June 1 for the summer tax levy or November 1 for the winter tax levy of the first year of the claim. A Conditional Rescission must be submitted to the assessor annually on or before December 31 to verify the property still complies with the conditional rescission requirements in order to receive the exemption for the following year.

In order to qualify for a conditional rescission, the owner must have purchased a second property in Michigan which is occupied as his or her principal residence. In addition, the previous principal residence must not be occupied, must be for sale, must not be leased, and must not be used for any business or commercial purposes in order for the owner to qualify for a conditional rescission.

Foreclosure Entity Conditional Rescission:

A land contract vendor, bank, credit union, or other lending institution (foreclosing entity) can retain a PRE on foreclosed property by filing a foreclosure entity conditional rescission with the local tax collecting unit on or before June 1 or November 1 provided the property meets other statutory requirements. If a foreclosure entity conditional rescission is timely filed and accepted for the first year, the foreclosing entity must annually verify to the assessor of the local tax collecting unit on or before December 31 that the property continues to qualify for the foreclosure entity conditional rescission. This new "foreclosure entity conditional rescission" has separate and distinct requirements and should not be confused with the current "owner's conditional rescission".

In order to qualify for a foreclosure entity conditional rescission, the following requirements must be met:

- The foreclosing entity must submit a Foreclosure Entity Conditional Rescission of Principal Residence Exemption by June 1 or November 1 of the first year of the claim.
- The foreclosure entity must be a land contract vendor, bank, credit union, or other lending institution.
- The foreclosure entity must own the property as a result of a foreclosure.
- The property must have been subject to a PRE immediately preceding the foreclosure.
- The property cannot be occupied.
- The property must be for sale.
- The property cannot be leased to any person other than the person who claimed the PRE immediately preceding the foreclosure.
- The property must not be used for any business or commercial purpose.
- The foreclosure entity must pay to the tax-collecting unit an amount equal to the amount of taxes that the foreclosing entity would have paid if the property were not subject to a PRE and must pay an administration fee equal to the property tax administration fee imposed under Section 44 of the General Property Tax Act.
- The foreclosure entity must annually verify the foreclosure entity conditional rescission by December 31.
- The foreclosure entity must rescind the exemption upon a transfer of ownership.

The payment required of the foreclosure entity is to be collected by the local tax collecting unit at the same time and in the same manner as taxes that would have been collected were the property not subject to a PRE. The payment must be distributed to

the Department of Treasury for deposit into the state school aid fund. The administration fee is to be retained by the local tax collecting unit. If the foreclosure entity fails to make the required payment, the local tax collecting unit must deny the foreclosure entity conditional rescission, retroactively, effective on December 31 of the immediately preceding year. If the foreclosure entity's conditional rescission is denied, the local tax collecting unit must remove the PRE and any additional taxes, penalties, and interest must be collected from the foreclosing entity.

Denial of a PRE:

Subsections 6, 8 and 11 of MCL 211.7cc allow the assessor, Department of Treasury (the Department), and in certain circumstances, the County Treasurer or Equalization Director, to deny PRE claims for the current and three preceding years. If an assessor believes that a property is not the principal residence of the owner claiming the exemption or that the owner failed to properly rescind the PRE, the assessor may deny the new or existing claim by notifying the owner using a Notice of Denial of Principal Residence Exemption, Form 2742 (Assessor's Denial). The Assessor's Denial provides the owner with his or her appeal rights to the Michigan Tax Tribunal (MTT) within 35 days from the date of the notice. The assessor does not need to seek the approval of the Board of Review when issuing a PRE denial.

MCL 211.7cc(11) gives the County Treasurer or County Equalization Director the authority to issue a denial notice. In order for the County to maintain the authority to deny a PRE claim, the County must elect to audit PRE claims in accordance with MCL 211.7cc(10). This election is made every five years. Notice of Denial of Principal Residence Exemption, Form 4075 (County's Denial), is issued by the County and provides the owner with his or her appeal rights to the MTT within 35 days from the date of the notice.

Under MCL 211.7cc(8), the Department is given the authority to deny PRE claims in any County in Michigan. The Department generally issues PRE denial notices by letter to the owner with a copy of the letter or list of denied parcels provided to the assessor, County Treasurer and the County Equalization Director. The owner has 35 days from the date the denial notice to appeal the denial to the Hearings Division of the Department. If the owner is not satisfied with the decision of the informal conference, they may then appeal the decision to the MTT

Qualified Agricultural Exemption: PA 237 of 1994

The Qualified Agricultural Property exemption is an exemption from 18 mills of local school operating millages for parcels that meet the Qualified Agricultural Property definition (MCL 211.7ee). Additionally a transfer of Qualified Agricultural Property is not considered a transfer of ownership if both of the following are true: The property remains Qualified Agricultural Property after the transfer and the new owner files Form 3676 with the assessor and the register of deeds.

A parcel that is classified agricultural normally receives the Qualified Agricultural Exemption automatically and the owner does not usually have to file Form 2599, Claim for Farmland Exemption from Some School Operating Taxes. However, the assessor can request the form to determine, for example, if the parcel contains structures that are not entitled to the exemption.

Owners of property not classified as agriculture must file form 2599 to receive the exemption. All owners must file form 2473, Request to Rescind Qualified Agricultural Property Exemption, to rescind the exemption within 90 days of a change that would cause rescission (e.g. change in use, change in ownership etc.). The requirement applies whether only a part, or all of the property, is affected. The penalty for not filing a rescission form is a maximum fine of \$200.

The exemption status is determined as of May 1st of the year of the exemption. Unlike the Principle Residence Exemption, property owned by a legal entity (such as a partnership, corporation, limited liability company, association, etc.) may receive the exemption. In some situations, land may not be actively farmed on May 1, yet the parcel containing the land may still be eligible for the exemption. For example, the land may be intentionally left fallow; the growing season for a crop in some parts of the state may begin after May 1, etc.

Qualified Agricultural Eligibility:

To be eligible for the exemption, a parcel has to be Qualified Agricultural Property. A parcel can become a Qualified Agricultural Property in two ways:

1. Classification of the parcel as agricultural on the current assessment roll or
2. Devotion of more than 50% of the acreage of the parcel to agricultural use as defined by law (MCL 324.36101).

The percentage of a parcel that is devoted to agricultural use is calculated based on the parcel's total acreage. Total acreage includes any area within the parcels ownership including any area(s) covered by an easement or right-of-way for road or drain purposes, even though the area under a public road right-of-way or a public (surface) drain right-of-way is exempt from taxation. Parcels classified agricultural do not have to have more than 50% devoted to agricultural use.

What is Agricultural Use?

The definition of "agricultural use" is contained in MCL 324.36101:

"Agricultural use" means the production of plants and animals useful to humans, including forages and sod crops; grains, feed crops, and field crops; dairy and dairy products; poultry and poultry products; livestock, including breeding and grazing of cattle, swine, captive cervidae, and similar animals; berries; herbs; flowers; seeds; grasses; nursery stock; fruits; vegetables; Christmas trees; and

other similar uses and activities. Agricultural use includes use in a federal acreage set-aside program or a federal conservation reserve program. Agricultural use does not include the management and harvesting of a woodlot.”

This definition of “agricultural use” differs from the definitions used to determine a parcel’s classification and should not be used in determining a parcel’s classification. There is no minimum parcel size and no minimum income from agricultural production needed to qualify. There are circumstances in which the land may qualify even though the land is not actively farmed. For example, the land may be left intentionally fallow or the growing season for a crop may begin after May 1st.

Denial of a Qualified Agricultural Exemption:

An assessor may deny:

- A new exemption, if the property or part of the property does not qualify
- An exemption continued from a prior year, at the time of preparation of the annual tax roll, if the property is no longer qualified
- An existing exemption after the close of the local Board of Review and up to the status day if the property is no longer qualified for the exemption and
- When the property owner has requested a withdrawal of the exemption for the current year, even if the request occurs after May 1st

If the assessor discovers a situation where it is clear that a parcel is incorrectly receiving the Qualified Agricultural Property exemption for the current year, after May 1, the assessor has no power to deny the exemption. The assessor may deny the exemption for the next year. Similarly, the assessor may not deny a Qualified Agricultural Property exemption for a prior year.

Qualified Forest Exemption: Public Acts 378, 379 and 380 of 2006

The Qualified Forest Program created an opportunity for owners of smaller forestland parcels in Michigan, which are not classified as agricultural land or do not receive a PRE, to receive reduced property taxes on land in productive, managed forests. The program exempts qualified property from certain school operating taxes and purchasers of QFP enrolled property may apply to the local unit to prevent a property’s taxable value from “uncapping” in the year following a transfer of ownership. MCL 211.7jj

Unlike the PRE, a QFP may be owned by a legal entity (such as a partnership, corporation, limited liability company, association etc.). This program is administered by the Department of Agriculture and Rural Development and more detailed information can be found on their website.

Exemption of Property Owned or Sold by a Land Bank Fast Track Authority: 211.7gg

Property owned by a Land Bank Fast Track Authority is exempt from ad valorem property taxes. When the Authority sells or conveys the property, it is still exempt from ad valorem property tax, but is subject to a specific tax levy. More information can be found at www.michigan.gov/lara.

Abatements

The term “**abatements**” refers to the following legislative programs: Industrial Facilities Tax (IFT) PA 198 of 1974; Neighborhood Enterprise Zone (NEZ) PA 147 of 1992; Obsolete Property Rehabilitation Act (OPRA) PA 146 of 2000; and Commercial Rehabilitation Act, PA 210 of 2005. The common legislative element is a “specific tax” which replaces the ad valorem tax. Characteristics of abatements that distinguish them from ad valorem taxation include: creation of the “specific tax” roll for improvements; leaving land to be assessed on the ad valorem tax roll and manipulation of either a millage rate or a property value.

Industrial Facilities Exemption, Public Act 198 of 1974

The Plant Rehabilitation and Industrial Development Districts Act (known as IFT), provides a tax incentive to manufacturers for: renovation and expansion of aging facilities, to assist in the building of new facilities, and to promote the establishment of high tech facilities. An Industrial Development District (IDD) or a Plant Rehabilitation District (PRD) must be created prior to initiating a project. An IFT Certificate entitles the facility to exemption from ad valorem real and/or personal property taxes for a term of 1-12 years as determined by the local unit of government. Applications are filed, reviewed and approved by the local unit of government, but are also subject to review at the State level by the Property Services Division and the Michigan Economic Development Corporation. The State Tax Commission (STC) is ultimately responsible for final approval and issuance of certificates. Exemptions are not effective until approved by the STC.

Commercial Rehabilitation Act, Public Act 210 of 2005

The Commercial Rehabilitation Act provides a tax incentive for the rehabilitation of commercial property for the primary purpose and use of a commercial business or multi-family residential facility. The property must be located within an established Commercial Rehabilitation District. Exemptions are approved for a term of 1-10 years, as determined by the local unit of government. The property taxes are based upon the previous year's (prior to rehabilitation) taxable value. The taxable value is frozen for the duration of the certificate. Applications are filed, reviewed and approved by the local unit of government, but are also subject to review at the State level by the Property Services Division. The State Tax Commission (STC) is responsible for final approval and issuance of certificates. Exemptions are not effective until approved by the STC.

Commercial Facilities Exemption, Public Act 255 of 1978

The Commercial Redevelopment Act (known as the Commercial Facilities Exemption), provides a tax incentive for the redevelopment of commercial property for the primary purpose and use of a commercial business enterprise. The property must be located within an established Commercial Redevelopment District. Exemptions are approved for a term of 1-12 years as determined by the local unit of government and the taxable value is frozen for the duration of the certificate. For restored facilities, the property taxes are based upon the previous year's (prior to restoration) taxable value and 100% of the mills levied. For new or replacement facilities, the property taxes are based upon the current year's taxable value and 50% of the mills levied. Applications are filed, reviewed, approved, and certificates are issued, by the local unit of government. Certificates are also filed with the State Tax Commission.

Obsolete Property Rehabilitation Act Exemption, Public Act 146 of 2004

The Obsolete Property Rehabilitation Act (known as OPRA), provides property tax exemptions for commercial and commercial housing properties that are rehabilitated and meet the requirements of the Act. Properties must meet eligibility requirements including a statement of obsolescence by the local assessor. The property must be located in an established Obsolete Property Rehabilitation District. Exemptions are approved for a term of 1-12 years as determined by the local unit of government. The property taxes for the rehabilitated property are based on the previous year's (prior to rehabilitation) taxable value. The taxable value is frozen for the duration of the exemption.

Additionally, the State Treasurer may approve reductions of half of the school operating and state education taxes for a period not to exceed 6 years for 25 applications annually. Applications are filed, reviewed and approved by the local unit of government, but are also subject to review at the State level. The State Tax Commission (STC) is responsible for final approval and issuance of OPRA certificates. Exemptions are not effective until approved by the STC.

Neighborhood Enterprise Zone Act Exemption, Public Act 147 of 1992

The Neighborhood Enterprise Zone Act (known as NEZ) provides for the development and rehabilitation of residential housing located within eligible distressed communities. New and rehabilitated facilities applications are filed, reviewed and approved by the local unit, but are also subject to review at the State level by the Property Services Division. The State Tax Commission (STC) is responsible for final approval and issuance of new and rehabilitated facility certificates. Exemptions for new and rehabilitated facilities are not effective until approved by the STC. NEZ Homestead applications are filed, reviewed and approved by the local unit of government.

Chapter 3 Valuation Concepts

Property assessments in Michigan use an “ad valorem” (at value) tax system. This means that taxes are based on property value. This value is determined by organizing and analyzing data to determine property value.

Section 27 (1) of the General Property Tax Act defines “true cash value” as “...the usual selling price at the place where the property to which the term is applied is at the time of assessment, being the price that could be obtained for the property at private sale, and not at auction sale except as otherwise provided in this section, or at forced sale.” The usual selling price does not include public auctions that are part of a liquidation of sellers assets in a bankruptcy proceeding nor does it include property sold at tax sale or the subsequent sale of property that is acquired by the state in the delinquent tax sale process.

The following definition of “market value” was adopted by the Appraisal Institute in 1993: “The most probable price which a specified interest in real property is likely to bring under all of the following conditions:

1. Consummation of a sale occurs as of a specified date.
2. An open and competitive market exists for the property interest appraised.
3. The buyer and seller are each acting prudently and knowledgeably.
4. The price is not affected by undue stimulus.
5. The buyer and seller are typically motivated.
6. Both parties are acting in what they consider their best interest.
7. Marketing efforts were adequate and a reasonable time was allowed for exposure in the open market.
8. Payment was made in cash in U.S. dollars or in terms of financial arrangements comparable thereto.
9. The price represents the normal consideration for the property sold, unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.”

When valuing property, the assessor should take into consideration the zoning of the property, the location of the property, the condition of structures on the property, the income potential of the property, and in farm areas the soil quality, value of standing timber, availability of water, and any mineral rights that are included in the ownership.

In order to have value the property must have the following (DUST):

1. **Desirability** – a consumer must want the product for it to have value.
2. **Utility** – the ability to satisfy as human want, need, or desire.
3. **Scarcity** – the present or anticipated supply of an item relative to the demand for it.
4. **Transferability** – a consumer must be able to purchase the property.

Real estate is the physical land and any structure attached to it.

Real property is the rights of ownership (bundle of rights) enjoyed by the owner of real estate.

The Bundle of rights are the rights obtained with fee simple title:

- S – Right to sell
- L – Right to lease or rent
- U – Right to use
- G – Right to give away
- E – Right to enter or leave
- R – Right to refuse to do any of these

The rights of ownership removed by government are:

1. Power to tax
2. Power of eminent domain
3. Police power – power to regulate
4. Escheat

The most common types of ownership are **fee simple** (the highest degree of ownership), **partial estate** (such as a leased property), and **life estate** (the right to use, occupy, and control a property for the length of the lessee's life).

Personal property includes movable items not permanently attached to the real estate. To decide if an item is real or personal consider the following:

1. The manner in which it is attached
2. The intention of the installer – to permanently attach or to eventually remove
3. The purpose for which the premises are used

The value of a property is not just the value you can obtain if you sell the property. The selling of a property is a value in exchange. The **value in exchange** is the amount of money or goods you can receive if you sell the property. Property also has a value in use. **Value in use** is the value property has in a specific use. Special purpose properties have a limited use. However they may have value to a user if they are redesigned or remodeled. Sometimes the value is greater if the limited use property is demolished and a new structure is erected. A limited use property is one that has a limited number of potential buyers due to the uniqueness of the property and the pool of buyers that could use it as it stands would be even more limited. Appraisals that include a value in use analysis will generally be large industrial buildings.

The basic economic principles used in appraising are as follows:

1. Supply and demand
2. Change
3. Contribution
4. Competition
5. Conformity
6. Anticipation
7. Substitution
8. Surplus productivity
9. Diminishing returns
10. Highest and best use

Highest and best use is the reasonably probable and legal use of vacant land or an improved property that is physically possible, appropriately supported, financially feasible, and that results in the highest value.

The appraisal process begins with defining value. The collection of physical data comes next. You need cost data on the specific site being appraised and also information on properties that have sold, government restrictions, and for income-producing properties, the potential income.

The three approaches to value are **cost, sales comparison, and income**. Each has specific applications.

The **cost approach** is used to estimate the cost of constructing improvements to the land. It is used when you do not have sufficient sales to compare, when the structure has just been built, and when you are doing mass appraisal. This approach is based on the principle of substitution.

The **sales comparison approach** compares the property being appraised to similar properties that have recently sold. Comparable properties are selected based on how similar they are to the subject. The sale price is adjusted for differences and a market value is estimated. Adjustment increases or decreases are made to the comps to make them equal to the subject property. This approach also is based on the principle of substitution.

The **income approach** is used to value the income stream of a property. This approach to value uses the principles of substitution and anticipation. Investors purchase properties based on the income that can be generated.

In reviewing the economic principles used in each approach, you can see that the one that is used in all three approaches to value is substitution. The principle of substitution states that a property's value tends to be set by the cost of acquiring an equally desirable substitute. This principle applies to all three approaches to value: in the sales comparison approach, the value of the subject property is determined by the cost of

purchasing a substitute property; in the cost approach, value is determined by the cost of constructing a similar substitute property; and in the income approach, value is determined by the cost of acquiring a substitute property that will provide a similar income stream. In each case, the substitute properties must be equally useful and desirable, and there must be no costly delays with either the purchase or construction.

The final reconciliation of value can be a combination of the approaches to value. The appraiser will decide which approach should be given the most weight.

In an assessing office the assessment process can be summarized as follows:

1. Locate and identify all taxable property
2. Inventory all property noting specific characteristics of each parcel
3. Estimate market value
4. Determine tax status – taxable or exempt
5. Calculate assessed, capped, and taxable values
6. Prepare certified assessment roll
7. Notify property owners of changes to their assessments
8. Defend values when appealed
9. Prepare tax roll

Chapter 4

Assessment Administration/Public Relations

The assessor's four basic duties are:

1. To inventory and list all property within the assessment jurisdiction.
2. To equitably evaluate every item of taxable property.
3. To calculate the taxable value for every taxable property.
4. To prepare an assessment roll with all taxable property listed in an orderly fashion by parcel number or legal description.

Calculating the taxable value requires eight steps to be sure the taxable value is legal and correct:

1. Determine taxability
2. Identify the owner
3. Describe the property accurately
4. Determine the "situs" (location) of the property
5. Value the property
6. Determine assessed value (50% of true cash value)
7. Determine capped value (Proposal A)
8. Determine taxable value (Proposal A)

In Michigan, the definition of **true cash value** is: "...the usual selling price at the place where the property to which the term is applied shall be at the time of the assessment, being the price which could be obtained therefore at private sale, and not at forced or auction sale. Any sale or other disposition by the state or any agency or political subdivision thereof heretofore or hereafter made of lands acquired for delinquent taxes or any appraisal made in connection therewith shall not be considered as controlling evidence of true cash value for assessment purposes. In determining the value the assessor shall also consider the advantages and disadvantages of location, quality of soil, zoning, existing use, and present economic income of structures, quality and value of standing timber, water power and privileges, mines, minerals, quarries or other valuable deposits known to be therein and their value."

Maintaining accurate property record cards is of primary importance. Assessors must have a system in place to keep track of changes to every parcel.

Assessing accuracy is the degree to which the property in the jurisdiction is assessed at a legally mandated and uniform percentage of market value.

Market value is the price at which a property would most likely sell in an open-market transaction involving a buyer and seller, both of whom desire to come to terms but are under no undue constraint to do so.

Assessment uniformity is the degree to which different properties are assessed at equal percentages of market value.

Assessment level is the overall ratio of assessments to market values and the degree to which this ratio meets the state mandated ratio.

Assessment efficiency refers to the cost of assessment operations; i.e., the number of appraisals per appraiser done each day and the percent of properties inspected. If the cost per appraisal is low then the assessment efficiency is high.

Cost effectiveness is demonstrated by a prudent use of all resources available.

An **assessment ratio study** is a statistical analysis of the degree of assessment accuracy. It determines the mean, median, and mode of the ratios. **Mean** is the simple average of the ratios. **Median** is the middle of a ratio study when the ratios are ranked from lowest to highest or highest to lowest. **Mode** is the value occurring most frequently in the data set.

Accurate property record cards and assessment maps are mandatory if you are to have an efficient office. Accurate maps insure that no property is omitted and no property is assessed twice. Remember, assessments are only as accurate as the data used to calculate them.

There are ten components to an effective assessment system. They are as follows:

1. Adequate budget, competent staff, and internal controls
2. Complete maps and files
3. Accurate property data
4. Accurate sales data
5. Effective cost approach
6. Effective sales comparison approach
7. Effective income approach
8. Modern data processing and storage
9. Open public relations
10. Periodic assessment-ratio studies

Components 1-4 are basic. If you do not have staff, you will not be able to maintain the records that are necessary to do the job. Components 5-7 relate to appraisal procedures and are necessary for accuracy. Component 8 is a means to efficiency in an assessing office. Component 9 is the golden rule. Component 10 is necessary to evaluate the accuracy of the records and to make necessary adjustments.

An important part of every assessor's job is good customer relations. It is important for assessors to remember that value of a home and the taxes due that result from that value are very emotional, regardless if the taxpayer is an individual or a company. There is a significant amount of stress involved in these issues. Put yourself in their

position. Think about how you would feel if you were upset over an issue and you did not receive a call back or received a call back and the individual on the other end was less than helpful. Think about how you would want to be treated; how would you want someone to explain the situation to you; what would you want them to do.

We do realize there are always going to be taxpayers that are rude and upset and will not listen to anything you have to say. Make sure you are always pleasant and professional. If they just will not listen, suggest that you put something to them in the mail and then they can call you again to discuss. This gives you an opportunity to take the time to send them something; some people do better seeing things in print; and it gives them time to calm down.

Taxpayers have the right to ask questions. They have the right to ask why. They have the right to ask questions regarding their neighbor's assessments. Don't ever forget that assessing records are open to the public and to their scrutiny. It is our job to respond to taxpayers questions in as thorough and professional manner as possible.

Taxpayers have a right to appeal. An appeal to the Board of Review or to the MTT or STC is not a personal attack nor is it a criticism of your work. We all do occasionally make mistakes. When confronted with information that shows you have made a mistake, accept the responsibility for your actions with professionalism.

It is also important to maintain a good working relationship with other public officials. These include: County and local unit Clerk, County and local unit Treasurer, Equalization Department, Township Trustees, City Council Members, local unit building inspector, local unit zoning inspector, MTT and STC.

Chapter 5 Equalization

Property taxes are a simple mathematical problem: Millage rate times the taxable value equals the taxes collected (revenue). This was a very simple math problem prior to Proposal A, when the value taxes were levied on was the state equalized value (SEV) also known as the assessed value (AV).

Proposal A requires the calculation of two additional values – the taxable value and the capped value. We now calculate the SEV/AV and the capped value. The lesser of the two becomes the taxable value (the value taxes are levied on).

Article 9, Section 3 of the Michigan Constitution of 1963, as amended, established the following five requirements of the legislature with regard to assessments and taxes:

1. Uniform general ad valorem taxation of real and tangible personal property.
2. The determination of true cash value of such property.
3. The proportion of true cash value at which such property shall be uniformly assessed (not to exceed 50% of true cash value).
4. Establish a system of Equalization of assessments.
5. Determine the taxable value of each parcel of property.

To accomplish these five requirements of the Constitution, the legislature, in the General Property Tax Act of 1893, established the following three levels of responsibility:

1. Local level (Assessor and Board of Review)
2. County level (Equalization department)
3. State level (State Tax Commission)

The assessing officer in the local government unit begins the process. He/she is required to establish the assessed and taxable value of all real and tangible personal property within the unit as of December 31 of each year (tax day).

All property is listed in an orderly manner in the assessment roll. For every property, the assessor determines the following:

1. The assessed value (50% of the true cash value).
2. The capped value (using the statutory formula and STC guidelines).
3. The taxable value (the lesser of the AV and capped values).

The assessor must complete their work by the first Monday in March, and must turn the roll over to the Board of Review (BOR) on the Tuesday following the first Monday in March.

The BOR is charged with making sure assessments are equitable and that values have been calculated properly. They also have the authority to change ownership records, legal descriptions, school district codes, property classification and, since 1994, homestead and qualified agricultural exemptions. The BOR hears appeals from property owners regarding their assessments, classification, and taxable status of property.

The BOR must complete its business on or before the first Monday in April. The BOR certifies the value of each class of real property separately and all classes of personal property as a whole.

When the certification and other required reports are completed, the assessor turns the roll over to the Equalization Department for County Equalization. The roll must be turned over by the Wednesday following the first Monday in April or 14 days following the adjournment of the Board of Review, whichever is earlier.

The County Equalization Director reviews each assessment roll in the County on behalf of the County Board of Commissioners. The Equalization Director summarizes the local units on form L-4411, Recommendation to the County Board of Commissioners. The County Board of Commissioners must begin their review on the Tuesday following the second Monday in April and must complete their work by the first Monday in May.

The Commissioners must determine whether the properties in each local unit have been equally and uniformly assessed. If they determine that an inequality exists, the Board is required by Statute to correct the inequality. This action does not affect the assessment rolls of the individual communities but may affect the final determination of taxable value for individual properties. When the County Board of Commissioners completes this process, they send form L-4044, Assessment Roll Certification of Equalization by County Board of Commissioners, to the local units and L-4024, Statement of Acreage and Valuation, to the State Tax Commission

The third level of the assessment/Equalization process is State Equalization. The State Tax Commission (STC) determines and establishes the uniform valuation of all classes of property between the 83 counties in Michigan. The STC has the authority to change any and all County equalized valuations if they do not reflect the constitutional maximum and statutory 50% level of assessment. The State Tax Commission issues its preliminary determinations on the second Monday in May and its final determination on the fourth Monday in May.

A right of appeal is provided at each level of this process. At the local level, individual property owners may appeal their assessment, their capped value, and taxable value as well as the classification of their property to the Board of Review. If they are not satisfied at the local level, they can appeal valuation issues to the Michigan Tax Tribunal and classification issues to the State Tax Commission.

Each local unit of government may appeal to the County Board of Commissioners if they do not agree with County Equalization. This will protect their right to appeal the County Equalization to the Michigan Tax Tribunal. Appeal of State Equalization is to the Court of Appeals.

Classification of Property

Property classification is defined in MCL 211.34c. Assessors are required to annual determine the classification for parcels in their jurisdiction. Following are the standard classifications of real and personal property:

Real Property

1. 100 Agricultural Real Property
2. 200 Commercial Real Property
3. 300 Industrial Real Property
4. 400 Residential Real Property
5. 500 Timber-Cutover Real Property
6. 600 Developmental Real Property

Personal Property

1. 150 Agricultural Personal Property
2. 250 Commercial Personal Property
3. 350 Industrial Personal Property
4. 450 Residential Personal Property
5. 550 Utility Personal Property

When classifying property for the assessment roll, assessors must be very careful with properties that may have more than one use. If a property has two uses (for example, a house and an auto repair business in an accessory building) the assessor must determine the use that most significantly influences the total valuation of the parcel. Another area where this is especially important is in areas where developers are purchasing agricultural property and subdividing it. The developer would like it to remain agricultural because of the benefits of Proposal A to agricultural property but it might be better classed developmental.

Assessors must be careful that they are assessing properties according to the definitions contained in MCL 211.34c. For the most part these definitions classify property according to the current use. While property is valued according to highest and best use, it is classified according to current use, using the definitions in MCL 211.34c.

Equalization Studies

Equalization departments are required to conduct Equalization studies for each class of property in the County. Real property studies use either a sales study or an appraisal study.

Sales Studies are typically done in the larger classes with adequate market transactions to accurately measure the assessment to value ratio. Most typical is the residential real class, although sales studies are also conducted in commercial, industrial, and agricultural classes in large units with large classes and adequate sales. Some small units might not have adequate sales to conduct any sales studies in any class and then would have to use an appraisal study.

Beginning in 2017 for use in the 2018 assessments, sales study dates are as follows:

- Two year study: April 1, two years prior through March 31, current year.
- Single year study: October 1, preceding year through September 30 current year.

All valid sales must be included and verified.

P.A. 162 of 2013 amended the requirements for sales to be included in agricultural sales studies and added an additional verification requirement:

(4) In finalizing sales studies for property classified as agricultural real property under section 34c, an assessor and equalization director shall determine if an affidavit for the property has been filed under section 27a(7)(n). If an affidavit has not been filed, the property shall be reviewed to determine if classification as agricultural real property under section 34c is correct or should be changed. The assessor for the local tax collecting unit in which the property is located shall contact the property owner to determine why the property owner did not file an affidavit under section 27a(7)(n). Unless there are convincing facts to the contrary, the sale of property classified as agricultural real property under section 34c for which an affidavit under section 27a(7)(n) has not been filed shall not be included in a sales study.

The same basic procedure is utilized in an appraisal study, except the “market value” is derived from an appraisal of the property rather than an open market sale. Due to a lack of sales in small units and/or tiny classes, this may be the only study approach for year after year.

Personal property studies are not done based on sales but rather on audits of a representative sampling of the personal property returns.

Chapter 6

Real Property Descriptions

In 1790, the Federal Northwest Ordinance established the laws that cover what are now Michigan, Ohio, Indiana, Illinois, and Wisconsin. The government land office was established to survey the territory. Since Michigan was still a wilderness, it is noteworthy that the maps done at that time were very good. Legal descriptions today use information established over 200 years ago. When we use the word "Township" in a discussion of descriptions, please keep in mind that the Townships we are referring to are not the political Townships that now exist. The Townships in this section are geographical Townships. They contain 36 sections, each a mile square.

The initial survey point for Michigan is in Genesee County at the intersection of two streets. The initial point was established and a meridian line would run true north and south from that point with a base line running east and west. These two lines would be the basis for laying out Townships. Townships would be numbered north and south from the base line. The first Township north of the base line would be called Town 1 North. Townships would also be numbered east and west of the meridian and would be known as ranges. The first Township east of the meridian would be called Range 1 East.

The rectangular survey method had been adopted which divides land into Townships 6 miles square and further divides a Township into 36 sections, each a mile square. Each section (1 square mile) would contain 640 acres. Using the town and range along with the section number or part of a section made it easy to locate property.

Because two surveyors were hired to do the surveys and each began at a different point, their initial points did not meet. Because settlers were already occupying the property based on one or the other of the surveys, a second initial point was established. There is a jog in the initial point between Jackson and Ingham Counties. The base line is the north boundary of Wayne County (Eight Mile Road) and runs across the state.

The assessor is charged with the duty of seeing that all real property in the governmental unit is assessed. To do so they must be able to identify and locate each property. The legal description does that.

There are three methods used to describe property in the state. The first is the rectangular survey or acreage description. It describes parcels by the section or subdivision of the section, town, and range as laid out by the original General Land Office survey.

The second method is metes and bounds. This describes parcels which are not a regular subdivision of a section or that are too small to be described as a subdivision of a section.

The third method is platted or recorded plat descriptions. This method describes land by lots and blocks after the area has been surveyed, platted, and recorded in the Register of Deeds office in the County and in Lansing.

One additional type of description exists in Michigan. Private claims describe property that was occupied prior to the General Land Office survey. These private claims are numbered and can be found along the waterways of the state.

To locate a rectangular survey, descriptions are read backwards. The first step is to locate the Principal or Michigan Meridian and the base line. The legal description contains the Town and Range of the property and the property can be located using the Base Line and Principal Meridian. The geographic Township is divided into fourths: the NE, NW, SE, and SW quadrants.

A rectangular survey is read backwards to map it. NE $\frac{1}{4}$ of NW $\frac{1}{4}$ of SE $\frac{1}{4}$, Section 32, T1N, R2E is mapped by locating the geographic Township, the section, and then the SE $\frac{1}{4}$ of the section. Within that quadrant, locate the NW $\frac{1}{4}$ and finally within that quadrant locate the NE $\frac{1}{4}$. You have located the 10-acre parcel described by the above legal description. Note: In actual assessment rolls, you may find the town, range, and section number at the beginning of the description because all the property in the political subdivision is in the same town and range.

All sections have 640 acres with the possible exception of the sections on the north and west sides of a survey Township. These sections may be called fractional subdivisions of a section and may contain more or less acres than are found in a standard section. Corrections were made in these sections to adjust for the earth's curvature and small errors in the original surveys. Correction lines are lines running east and west parallel to the base line that set new corners for the Townships, again to adjust for the earth's curvature.

Sections may be divided into halves, quarters, or smaller parts of the original section. A half-section would be 320 acres and a quarter-section would be 160 acres. The description would describe half of the section as the N $\frac{1}{2}$ of Section 1; the S $\frac{1}{2}$ of Section 1; the E $\frac{1}{2}$ of Section 1; or the W $\frac{1}{2}$ of Section 1; depending on how the section was divided. If the section were divided into four parts, it would be NE $\frac{1}{4}$, SE $\frac{1}{4}$, NW $\frac{1}{4}$, or SW $\frac{1}{4}$.

"Metes" means to measure and "bounds" stands for boundaries, therefore a measurement of boundaries on a parcel. This method is used to describe shapes of land other than rectangular. There are 360 degrees in a circle and there are 60 minutes in a degree and 60 seconds in every minute. Knowing the divisions will enable a person to understand metes and bounds descriptions. Using a protractor or land compass is necessary for mapping a metes and bounds description. North and south are zero degrees and east and west are 90 degrees. If the description states N 89' E 200 feet, that dimension would be drawn using the rounded side of the protractor placed to the East. An engineer's scale should be used to measure the distances. There are a

number of different ways to describe the same parcel of land so always map the description to identify the parcel.

Five important measurements you will need to know when working with descriptions are:

16 ½ feet = 1 rod

36 square miles = a survey Township

640 acres = 1 section

5,280 lineal feet = 1 mile

43,560 square feet = 1 acre

Computation of areas may be done using the following formulas:

Rectangular – Length times the width

Triangle – Half the base times the height

Circle – Radius squared times Pi (3.1416)

The unknown dimension formula is as follows:

Number of acres times 43,560 divided by the known dimension

Remember, public rights-of-way are exempt, so remove that acreage before the assessment value is determined.

It is also important to know that sections in a Township start in the northeast corner with section 1 and proceed west to section 6. Section 7 is due south of section 6 and the numbers go east through section 12. This process is continued for all 36 sections with section 36 being the last section in the southeast corner of the Township.

6	5	4	3	2	1
7	8	9	10	11	12
18	17	16	15	14	13
19	20	21	22	23	24
30	29	28	27	26	25
31	32	33	34	35	36

Chapter 7 Vacant Land Valuation

Vacant land is not reproducible, so an estimate of its value must be made from the sales prices of other parcels of land similar to the property being appraised. Adjustment may have to be made for differences in:

1. Financial terms of Sale - Down payment, repayment, and interest rate
2. Time of sale - Inflation and economic conditions
3. Location
4. Physical differences - Size, shape, view, and soil type
5. Restrictions of use - Zoning, building codes, and deed restrictions

Adjustment can be made using dollar amounts or by using a percentage. The property with the smallest number of adjustments is the best comp.

The steps in appraising vacant land are as follows:

1. Identify type of adjustment necessary
 - a. Financial terms of the sale
 - b. Time of sale
 - c. Location
 - d. Physical differences
 - e. Use restrictions
2. Make adjustments
 - a. Plus if the comparable is less desirable than subject
 - b. Minus if the comparable is more desirable than subject
3. Examine subject and make an appraisal card
 - a. Sketch of the lot with dimensions
 - b. Improvements or special features
 - c. Prior sales of subject
4. Locate and examine comparable sales
 - a. Verify the sales with parties to the sale
 - b. List differences between lots
5. Adjust comparable sales as listed in 1 & 2 above
6. Select best indicator of value; usually property most similar to subject.
7. Determine value of subject

Land Value Maps

Land value maps are a graphical presentation of land values for an entire assessment unit (i.e., an entire City or Township). A graphical display of land values enables the assessor to explain and defend the results of his or her land value analyses to taxpayers. Constructing land value maps also helps keep the assessor informed of land value changes or patterns in the assessment jurisdiction. Significant information which might not otherwise be noticed often becomes apparent when land value information is presented graphically.

MCL 211.10e requires that assessors maintain land value maps consistent with the standards provided in the State Tax Commission's Assessor's Manual. Land value maps are defined in the Assessor's Manual as "maps on which are recorded the front or square foot value of platted property and the square foot or per acre value of acreage property." A good set of land value maps will contain both, the value conclusions for land used by the assessor to determine assessments, and the vacant land sales information used by the assessor to reach those conclusions. This may take the form of two sets of maps (one with sales information and the other with the assessor's value conclusions). It is a good practice to have individual land value maps, or color coded at a minimum, for different classes of property such as agricultural, residential, commercial, etc.

To set up a land value map system, you have to put together a set of maps for the entire assessing district. Types of maps that can be used include, but are not limited to, copies of tax maps; copies of recorded plats of subdivisions; City, Township, and County street maps; aerial photographs with map overlays; and zoning and land use maps. Maps need to be at a useful scale. Once a set of maps has been put together, known vacant land sales information which has been verified should be added to the maps. The sales information should be put on the map in an appropriate unit of comparison for the type of property involved. The land value conclusions of the assessor should also be added to the maps. This information will enable a property owner to see how his or her land has been valued as well as the supporting information behind that valuation. This graphical presentation can be extremely helpful in explaining and defending assessments.

Depth Factor

A depth factor is used, usually in urban or suburban settings, to adjust land value for differences in the actual depth of a parcel compared to the standard or typical depth for an area. A lot that is deeper than the standard depth lot will usually have more value and a lot that has less depth than the standard lot will usually have less value. Depth factors allow for a uniform amount per front foot to be used to value parcels of different depths by adjusting for differences in depth by converting actual frontage into equivalent front feet. This equivalent frontage, multiplied by the established front foot value, gives the appraised value of the lot.

Depth factor tables can be used instead of calculating individual depth factors for each parcel being valued. If a depth factor table is used, the resulting values should be checked against market information to ensure that the table is appropriate for the area being valued. When using a depth factor table (reprinted from the STC manual), it should be kept in mind that a given depth factor table will not work in all valuation situations.

Figure 36

DEPTH FACTOR TABLE

Actual Depth of Lot	Standard Depth of Lot					
	100'	110'	120'	130'	135'	150'
5'.....	22	21	21	20	19	18
10'.....	32	30	29	28	27	26
15'.....	39	37	35	34	33	32
20'.....	45	43	41	39	39	37
25'.....	50	48	46	44	44	41
30'.....	55	52	50	48	47	45
35'.....	59	56	54	52	51	48
40'.....	63	60	58	56	55	52
45'.....	67	64	61	59	58	55
50'.....	71	67	65	62	61	58
55'.....	74	71	68	65	64	61
60'.....	78	74	71	68	67	63
65'.....	81	77	74	71	69	66
70'.....	84	80	76	73	72	68
75'.....	87	83	79	76	75	71
80'.....	89	85	82	78	77	73
85'.....	92	88	84	81	79	75
90'.....	95	91	87	83	82	78
95'.....	98	93	89	86	84	80
100'.....	100	95	91	88	86	82
105'.....	103	98	94	90	88	84
110'.....	105	100	96	92	90	86
115'.....	107	102	98	94	92	88
120'.....	110	104	100	96	94	89
125'.....	112	107	102	98	96	91
130'.....	114	109	104	100	98	93
135'.....	116	111	106	102	100	95
140'.....	118	113	108	104	102	97
145'.....	120	115	110	106	104	98
150'.....	123	117	112	108	105	100
155'.....	125	119	114	109	107	102
160'.....	127	121	116	111	109	103
165'.....	129	123	117	113	111	105
170'.....	130	124	119	114	112	106
175'.....	132	126	121	116	114	108
180'.....	134	128	123	118	116	110
185'.....	136	130	124	119	117	111
190'.....	138	131	126	121	119	113
195'.....	140	133	128	123	120	114
200'.....	141	135	129	124	122	115

The depth factor table has been modified to eliminate decimals.

Agricultural Property

Every County in Michigan has agricultural property. It is important that all assessors understand agricultural valuation principles so they also understand how the Equalization process works when comparing urban and rural communities.

The General Property Tax Act states that agricultural operations means farming in all its branches. Included in the classification are cultivating soil, growing and harvesting commodities, dairy farming, raising livestock, bees, fish, fur-bearing animals, and poultry. The law includes turf and tree farming and any practices that are incidental to these farming operations.

Since farmlands are constantly being developed for other purposes, the assessor in an agricultural area must be aware of what agricultural property is being sold for in terms of money and also if it is being sold for agricultural use or for development.

When appraising agricultural lands, it is important to compare similar properties. If the property is a dairy farm, the comparables should be dairy farms. If it is a cash crop operation, it should be compared to other cash crop farms. Using the appropriate comparables will avoid comparing farmland that is being farmed to agricultural property that is being converted to residential or other uses.

All three approaches to value may be used in the appraisal process but the income approach is usually not used due to the difficulty of establishing an accurate income stream. Valuing farmland is usually done by the sales comparison approach for the land values and the cost approach for the buildings.

When valuing agricultural land, there are special factors that must be considered. General factors are length of growing season, rainfall, location of market, location of transportation, and topography.

Specific factors include productivity of soil, slope, drainage/water supply, size/shape of the parcel, and management practices. Some land may be suited for one type of crop but not for another. The assessor must be aware of these factors when developing land values. Field inspection is very important in valuing farmlands. The assessor should make every effort to visit the farms in his/her area and interview the owners. Usually the owners are very aware of things going on that will have an impact on the land values.

Soil survey maps can be obtained from the County extension service or from the U.S.D.A. Soil Conservation Service. These maps will indicate the location of various types of soil, which is important when valuing agricultural land.

Land value maps that contain the sale price and the type of soil on that parcel will be very helpful in determining land values. Land value grids and aerial photos are also useful tools.

Land value in agricultural districts is also dependent on the soil productivity ratings. Number 1 soil is considered the most productive soil and has a 100% productivity rating. The remaining soils are ranked in proportion to their productivity. In counties where there are agricultural activities, the Equalization department will have developed productivity rating charts for the soils found in their counties.

Homes on farms are priced from the Assessor's Manual just as any other home would be. Other farm buildings and improvements are usually classified as:

1. Typical farm buildings, which include pole buildings, silos, and large grain bins.
2. Obsolete farm buildings, which include hen houses, small grain bins, and buildings that are too small for modern machinery or whose original purpose is no longer necessary.
3. Special purpose buildings, which include buildings where temperature and humidity control are vital to the farming operation.
4. Drainage tile.
5. Irrigation systems. Movable irrigation systems including the pumps which are not an integral part of a well are agricultural personal property and are exempt.
6. Wells and septic systems.

Proper application of the costs in the Assessor's Manual along with application of appropriate multipliers will result in an accurate assessment.

Public Act 116 of 1974, known as Farmland and Open Space Preservation Act, allows farmers to place their property in a program that provides for a tax credit on their income tax. There are specific guidelines that must be followed and penalties for withdrawing from the program. This program is administered by the Department of Agriculture.

Forest/Timberlands

The definition of timber-cutover (from Section 211.34c(2)(f)) is: "Timber-cutover real property includes parcels that are stocked with forest products of merchantable type and size, cutover forest land with little or no merchantable products, and marsh lands or other barren land. However, when a typical purchase of this type of land is for residential or recreational uses, the classification shall be changed to residential."

An indication that wooded lands should be classified as other than timber-cutover are buildings on the land.

Included in the definition of "true cash value" is the statement that the assessor should consider the quantity and value of standing timber. This does not mean that because there is a large wooded area this is timberland.

Timberland usually includes parcels that are stocked with forest products of merchantable type and size not used for suburban or urban purposes. Cutover land usually has little or no commercially merchantable products. The original forest has been partially or completely removed.

Valuation of timber-cutover property is accomplished by following these four general procedures:

1. Determine the type or class of land.
2. Determine the type and extent of cover.
3. Determine the present and anticipated utilization of the parcel.
4. Estimate property values by comparing with similar properties.

Forestland valuation schedules must be developed for each region and must be constructed from transactions that have been verified. If there are not sufficient sales, a preliminary schedule may be developed by analysis of factors affecting land values.

Components that make up value in forestlands include:

1. Merchantable timber. What will the various types of timber sell for?
2. Reproduction. There is no market for seedlings and sapling even though there is a value when full growth is attained.
3. Mineral. Unless you are certain the timber is over mineral fields, this should be ignored.
4. Bare land. The value of bare land is a guess. It has value as a growing area for trees but as bare land the value is very uncertain.

Management costs are an important component in timber-cutover. Taxes are probably the largest expense in this classification and provisions have been made via the Commercial Forest Act to reduce taxes. The CFA replaces ad valorem taxes with a lower specific tax.

It is important that owners be aware of boundary lines and any encroachments onto their property. Adverse possession (a method of acquisition of title by possession) could take years to settle in court.

There should be a definite forest management program in place. The property should be inspected on a regular basis and the owner or manager should keep up-to-date on new improvements and discoveries.

When dealing with timber-cutover, you need to understand forest management. The assessor should be able to determine types of trees from aerial photos. He/she should also keep property record cards with at least a map of the property showing roads, trails, water, soil types, and timber types.

The Private Forest Reserve Act is an act designed to encourage private forestry. This act allows property owners who have an agricultural use on half their property to designate a specific number of acres as a Private Forest Reserve. The portion in the reserve is taxed on the ad valorem roll at an assessed value of \$1 per acre. When the timber is harvested, the owner pays a fee of 5% of the stumpage value for the timber removed. If they wish to withdraw from the program, the local assessor will determine the stumpage value of the timber on the land and the owner is required to pay a fee of 5% of this appraised value.

Applications are made for this program to the County Treasurer and they in turn notifies the local Supervisor who will determine if the land is in compliance with the requirements of the act.

Chapter 8 Taxable Value

Article 9, Section 3 of the Michigan Constitution provides for uniform property taxation except taxes levied for school operating purposes. Since Proposal A passed, there are different millages for school operating purposes for homestead and non-homestead properties. These uniform assessments are not to exceed 50% of true cash value as equalized. Article 9 limits the increase in taxable value to the increase in the consumer price index (CPI) or 5% whichever is less until the ownership of the property transfers.

When ownership of the property is transferred as defined by law, the parcel shall be assessed at the applicable proportions of current true cash value (50%). This value is not ½ the selling price.

Effective February 1, 1994 there is a limit on the maximum amount of ad valorem property taxes that may be levied for school district operating purposes. To change this amount requires approval of ¾ of the members of the Senate and House of Representatives.

All of the constitutional and Michigan property tax laws dealing with State and County Equalization that require properties to be uniformly assessed at 50% of true cash value (the usual selling price) are still in effect. Proposal A did not change this requirement.

Assessors are required to prepare an assessment roll containing uniform values for each property at 50% of true cash value. The legislature has defined true cash value as the usual selling price of property.

Assessors are required to annually estimate the true cash value of each parcel and establish an assessment based upon that estimate. Assessing officials are not to multiply assessments across the board neither by a tentative Equalization factor nor by the most recent consumer price index or inflation rate multiplier (IRM) to establish assessed values in the roll.

The constitutional cap on annual increases in taxable value does not apply to increases in assessed values. Assessed values will be adjusted annually to reflect the market in each area.

County and State Equalizations of assessments are still required. If a County Board of Commissioners determines that the assessments in a class of property are less or more than 50% of value, they must equalize the assessments by adding or subtracting an amount that will produce a sum that represents the true cash value of that class of property.

The State Tax Commission is also required to review the County equalized values and, if necessary, make such adjustments that will produce a sum representing the true cash value of that class of property.

The Michigan Constitution limits the taxes on a property by limiting the assessed value of a property at 50% of its true cash value. Proposal A required the calculation of a capped and taxable value in addition to the assessed value.

Taxable Value

PROPERTY TAXES = TAXABLE VALUE x AUTHORIZED MILLAGE RATE

Proposal A placed a cap on increases in taxable value for every parcel. There is an exception for property whose ownership has transferred. Beginning with the 1996 tax year, properties where ownership has transferred are “uncapped.” This uncapping is still subject to the 50% of true cash value constitutional requirement. This is why we must still calculate an assessed value each year for each property. When the property transfers, the assessed value becomes the taxable value for the following year. It is then recapped until the next transfer of ownership.

Under specific circumstances, it is possible that the SEV could become the taxable value even if the property does not transfer. The law states that the taxable value is the lesser of the SEV or the capped value. When the capped value is compared to the SEV, if the SEV is lower, it will become the taxable value.

The following examples are a property with no physical changes. The true cash value (TCV) of the property was \$100,000. Last year’s taxable value was \$49,000. Prior year’s SEV was \$50,000. The market value increase was 4% and the IRM was 1.024.

The assessor must calculate the SEV for next year.

True Cash Value of the Property	\$100,000
Market Value Increase	4,000
True Cash Value	104,000
SEV	52,000

The assessor must calculate the capped value.

Prior Year’s Taxable	\$49,000
Minus Taxable Value of Losses	-0-
Times the Lesser of 1.05 or the IRM	1.024
Plus Taxable Value of Additions	-0-
Equals the Capped Value	50,176

Since the capped value of \$50,176 is less than the SEV of \$52,000, the taxable value will be \$50,176.

The capped value formula is:

Current Year Capped Value = (Prior Year Taxable Value – LOSSES) X IRM + ADDITIONS

The prior year's taxable value is the value used in the immediately preceding year to calculate that year's property taxes.

July or December Board of Review changes and Michigan Tax Tribunal changes to the prior year's assessed, equalized, or taxable values may change the taxable value in the prior assessment or tax rolls. A new prior taxable value based on the Board of Review and MTT action must be used as the beginning value in the capped value formula to correctly calculate taxable value for the current year.

See the Annual STC Bulletin Regarding the Inflation Multiplier and Capped Value Formula:

Note: The Calculation of the Inflation Rate Multiplier is set in statute. MCL 211.34d states:

(l) "Inflation rate" means the ratio of the general price level for the state fiscal year ending in the calendar year immediately preceding the current year divided by the general price level for the state fiscal year ending in the calendar year before the year immediately preceding the current year.

(f) "General price level" means the annual average of the 12 monthly values for the United States consumer price index for all urban consumers as defined and officially reported by the United States department of labor, bureau of labor statistics.

Local units cannot develop or adopt or use an inflation rate multiplier other than that adopted by the State Tax Commission. It is not acceptable for Local units to indicate to taxpayers that you do not know how the multiplier is developed.

Tentative Taxable Value

Assessors are required to calculate a capped value for each parcel of real property. This capped value is compared to the SEV and the lesser of the two will become the taxable value. This is the value that taxes are levied on.

Until the STC adopts final Equalization in May, all values are tentative.

The assessment roll must contain the name and address of the person liable for the taxes, a description of the property, the tentative assessed, capped, and taxable values. The assessor is required to notify each person on the assessment roll (a notice by first class mail) of any increase in assessed value or taxable value. This notice is to be sent 14 days prior to the first meeting of the Board of Review. The STC recommends that

change notices be sent to all taxpayers even if there is a reduction in taxable value or assessed value

The only time it may be necessary to recalculate assessed, capped, and taxable values would be if the County Board of Commissioners or the State Tax Commission changed the tentative Equalization factor originally used.

The assessor has the authority to change taxable value in two circumstances:

1. If the unit receives a County or State Equalization factor that is more or less than the tentative factor.
2. If a transfer of ownership is received after adjournment of the March BOR and the taxable value has not been uncapped due to the failure of the new owner to file a Property Transfer Affidavit with the assessor.

Assessors do not have the authority to correct errors in loss or addition to the capped value. These errors can only be corrected if there is statutory authority such as appeals to the MTT, Section 154 appeals to the STC, or a Section 53b clerical error, mutual mistake of facts or qualified error, which can be corrected by the July or December BOR.

Loss, Losses, New and Additions:

The term “new” is used to describe added true cash value for property which is described for the first time on the assessment roll or which was formerly exempt from taxation. “New” would include value added for a new piece of equipment, a new building, a new structure (including value added for completion of construction for a structure which was partially valued in a prior year), etc. “New” also includes value added for the platting of land and value added for a change in a parcel’s description (e.g., a combination of two parcels).

The term “loss” is used in assessment administration to describe assessment decreases resulting from reduced true cash value because property was removed from the assessment roll (i.e., annexed to another assessment unit), because property was destroyed or became exempt from taxation, or because property was removed from a parcel description (e.g., split from a parcel). “Loss” also includes a reduction in the assessed value of personal property because the value of the personal property decreased compared to the prior year.

The terms “additions” and “losses” are used in assessment administration to mean increases and decreases, respectively, in the capped value formula, according to statutory definitions. The term “additions” includes value added for omitted property, new construction, previously exempt property, replacement construction, and remediation of environmental contamination. The term “losses” includes value reductions for property destroyed or removed, property which has become exempt from taxation, property which has experienced a decrease in value due to decreased occupancy rates, and property which has experienced a decrease in value due to

environmental contamination.

The term “adjustment” refers to positive or negative changes (i.e., plus or minus adjustments) made for the Equalization process. Technically speaking, “adjustment” covers all assessment increases or decreases other than the changes covered by “new” or “loss.” “Adjustment” is commonly considered to be a change in value to set assessments at 50 percent of true cash value as required by law.

Please see the table below that describes how each item defined above affects assessed or capped value. As a rule of thumb, 95% of the time you will have a new with an addition or a loss with losses. They simply affect different values on the roll. However, there are some circumstances when you will have new or loss but not additions or losses. These would include things like: splits, combinations, platting, and annexation. It is important that assessors understand these terms as they are critical to the understanding of the relationship between assessed and taxable value.

Term	Affects Assessed Value/SEV	Affects Capped Value
New	Yes	No
Loss	Yes	No
Additions	No	Yes
Losses	No	Yes
Adjustment	Yes	No

Examples of New and Additions

1. Omitted property
2. New construction.
3. Previously exempt property.
4. Replacement construction.
5. Remediation of environmental contamination.

The following are not additions for the capped value formula or in determining millage reduction fractions or base tax rate fraction:

1. Platting, splits, or combinations
2. Zoning changes.
3. Inflation.
4. Economic conditions.

Examples of Loss and Losses

1. Property that is destroyed or removed.
2. Exempt property.
3. Decrease in occupancy rate.
4. Environmentally contaminated property.

Value decreases that are not losses in value to the capped value are:

1. Platting, splits, or combinations.
2. Zoning changes. Do not confuse zoning changes with assessment classification changes.
3. Deflation.
4. Economic conditions.

Transfers of Ownership

When ownership of the parcel is transferred as defined by law, the property shall be assessed at the applicable proportion of true cash value for the year following the transfer.

This does not mean that the assessment is set at 50% of the selling price. It does mean that the SEV (after market adjustments) will be the assessed, capped, and taxable value the year following the sale. It is then recapped until the next transfer of ownership. Following are examples of transfers of ownership.

“Transfers of Ownership”

1. Deed
2. Land contract
3. Conveyance to a trust (unless beneficiary is same as settlor)
4. Distribution from a trust
5. Change in beneficiary of trust
6. Distribution after owner dies
7. Lease
8. Corporation partnership
9. Tenancy in common

NOT “Transfers of Ownership”

1. Spouse to spouse
2. Tenancy by entireties
3. Life lease
4. Foreclosure/forfeiture
5. Redemption – forfeited land for non-payment of taxes
6. Conveyance to trust when beneficiary is same as settlor
7. Court order
8. Joint tenancy
9. Security interest
10. Affiliated group
11. Normal public trading
12. Common control
13. Tax free reorganization
14. Relationship by first degree of blood or affinity to the first degree

Transfers of ownership occurs:

1. Date the deed or land contract is delivered to buyer.
2. Usually the same date the deed or land contract is signed.
3. Frequently not the same date as the document is recorded with Register of Deeds.
4. Usually not the same as the date of offer to purchase.

Transfers are reported to the assessor's office using the Property Transfer Affidavit Form (PTA), Form L-4260 within 45 days after the transfer of ownership.

If a PTA is not timely filed and the assessor believes a transfer took place, he/she must immediately send out a form to the new owner. If there was a transfer, he/she must immediately "uncap" the property and enter new taxable value on assessment and tax rolls. The property owner has 35 days to appeal to MTT. The assessor must notify the treasurer of the additional taxes due. If tax bills have been sent, the treasurer must immediately send a corrected tax bill including penalty and interest.

For real property classified other than industrial real or commercial real, Michigan law provides a penalty of \$5.00 per day for each separate failure to file a Property Transfer Affidavit up to a maximum of \$200.00. For property classified commercial real or industrial real with a sales price of \$100 million or less the penalty is \$20 per day up to a maximum of \$1,000. For property classified commercial real or industrial real with a sales price over \$100 million the penalty is \$20,000 unless the taxpayer can demonstrate that the failure to file was due to reasonable cause and not due to willful neglect. If the taxpayer can make that demonstration then the penalty is \$20 per day up to a maximum of \$1,000. Penalties begin to accrue after the 45-day filing deadline has passed. However, the governing body of a local unit of government may adopt a resolution waiving this penalty.

Chapter 9 Personal Property

Assessors are required to mail personal property statements (Form 632) by January 10th each year. All owners or possessors of assessable personal property are required to file a Personal Property Statement (Form 632) annually, no later than February 20, with the assessing officer of the unit where the property has situs, unless they are Eligible Manufacturing Personal Property or subject to the Small Business Taxpayer Exemption (discussed below). Situs is the location of the personal property on tax day, December 31, of each year. The owner is required to file on forms prescribed or approved by the State Tax Commission.

In December of 2012, initial legislation was passed that significantly changed the taxation of personal property. This legislation has been updated twice since the original passage. The Acts exempt personal property from taxation through two main provisions: Small Business Taxpayer Exemption (MCL 211.9o) and Eligible Manufacturing Personal Property Exemption (MCL 211.9m and MCL 211.9n). The Acts also identified a replacement specific tax on personal property (Essential Services Assessment) and reimbursement for local units lost revenue.

The Small Business Taxpayer Exemption (MCL 211.9o) had an effective date of December 31, 2013 for the 2014 tax year. MCL 211.9o includes an exemption for eligible personal property which is defined as:

1. Personal property classified as industrial personal property or commercial personal property as defined in MCL 211.34c or would be classified as industrial personal property or commercial personal property if not exempt **and**
2. The combined true cash value of all industrial personal property and commercial personal property owned by, leased by or in the possession of the owner or a related entity claiming the exemption is less than \$80,000 in the local tax collecting unit **and**
3. The property is not leased to or used by a person that previously owned the property or a person that, directly or indirectly controls, is controlled by, or under common control with the person that previously owned the property.

Beginning in 2019, taxpayers are no longer required to annually file Form 5076 in order to claim the exemption. Taxpayers who file Form 5076 and are granted the exemption will continue to receive the exemption until they no longer qualify for the exemption. At that point, the taxpayer is required to file a rescission form and a personal property statement no later than February 20th of the year that the property is no longer eligible. Failure to file the rescission form will result in significant penalty and interest as prescribed by P.A. 132 of 2018. An owner who fails to file a rescission and whose property is later discovered to be ineligible for the exemption is subject to repayment of

any additional taxes with interest at a rate of 1% per month or fraction of a month and penalties compute from the date the taxes were last payable without interest or penalty.

If a taxpayer has identified that they are subject to the Small Business Taxpayer Exemption, they do not have to file Form 632. See the Assessors Guide to the Small Business Taxpayer Exemption on the STC website for more information.

Effective December 31, 2015 for the 2016 year, Qualified New Personal Property and Qualified Previously Existing Personal Property is exempt from taxation.

Qualified New Personal Property (MCL 211.9m) is defined as property that was initially placed in service in this state or outside of this state **after** December 31, 2012 or that was construction in progress on or after December 31, 2012 that had not been placed in service in this state or outside of this state before 2013 **and** is eligible manufacturing personal property (EMPP).

Qualified Previously Existing Personal Property (MCL 211.9n) means personal property that was first placed in service within this state or outside of this state more than 10 years before the current calendar year **and** is eligible manufacturing personal property (EMPP).

Key to both of these definitions is that the Qualified New or Qualified Previously Existing personal property must be Eligible Manufacturing Personal Property.

Eligible Manufacturing Personal Property (EMPP) is defined as all personal property located on *occupied real property* if that personal property is *predominantly used in industrial processing or direct integrated support*. For personal property that is construction in progress and part of a new facility not in operation, EMPP means all personal property that is part of that new facility if that personal property will be *predominantly used in industrial processing* when the facility becomes operational. Personal property that is not owned, leased or used by the person who owns or leases *occupied real property* where the personal property is located is not EMPP unless the personal property is located on the *occupied real property* to carry on a current on-site business activity. Personal property that is placed on *occupied real property* solely to qualify the personal property for an exemption under 9m or 9n is not EMPP.

A more specific definition of EMPP including definitions of occupied real, predominantly used and industrial processing and direct integrated support is found in Bulletin 7 of 2015.

These exemptions will phase in beginning in 2016 until 2023 when all Eligible Manufacturing Personal Property is exempt.

Taxpayers who are EMPP will claim the exemption by filing Form 5278 with the local unit assessor. This form contains the affidavit stating the property is EMPP, the

personal property statement and multipliers for EMPP that, during the phase in, is assessed on the Ad Valorem roll and the Essential Services Assessment Statement.

The Essential Services assessment is a State specific tax on eligible personal property. In effect this is a specific tax replacement for the personal property tax. Although this is a specific tax assessed and collected by the State of Michigan, assessors need to be aware of the components of the tax and the rescission provisions.

Finally, the statutory changes affected some special act exemptions. These changes require that some specific exemption certificates remain in effect (are extended) until the EMPP exempted in these certificates become exempt under MCL 211.9m or MCL 211.9n.

More information on EMPP and ESA can be found in the Assessor's Guide to EMPP and ESA available on the STC Website.

Each year, the Assessor must mail a copy of the approved Personal Property Statement (Form 632) by January 10, to every known owner or possessor of assessable personal property. MCL 211.23 requires that all of Form 632's received by the supervisor or Assessor shall be made available to the County Equalization Department.

If February 20 is a Saturday, Sunday or legal holiday, Form 632 is due on the next business day after February 20. Form 632 must be received, not postmarked, by the Assessor by the due date. Assessors cannot require filing earlier or later than February 20. One exception is requirement that a "qualified business" who wants to have "qualified property" assessed to the user rather than to the owner file by February 1. An Assessor has no statutory authority to extend the filing deadline.

If a taxpayer has identified that they are EMPP, they will file Form 5278 to claim the exemption. Assessors are not required to mail Form 5278 to taxpayers. If a taxpayer identifies themselves as EMPP, they are required to obtain Form 5278 from the PPT website and file that form with the local unit where the personal property is located.

Generally, a taxpayer does not owe personal property tax in the tax year assessable personal property is first placed in Michigan. The taxpayer must file Form 632 by February 20 of the first calendar year after it moves assessable personal property into Michigan. However, the taxpayer should provide written notification to the Assessor(s) in the assessment jurisdiction(s) where assessable personal property is situated, notifying them of the address of the business location in that jurisdiction, the business operating name, the legal business name (if different from the operating name) and the correct mailing address for notices and billings.

If an Assessor sends Form 632 to the owner and it is not completed and returned, the Assessor is required to make an estimated assessment, unless the taxpayer has identified their property as EMPP and filed Form 5278 or have filed the Small Business Taxpayer Exemption Affidavit (5076). If a completed Form 632 cannot be obtained from

a person or entity, or if the Assessor is aware that a Form 632 is incorrect, the Assessor may examine under oath a person having knowledge of the Taxpayer's property and is authorized to make an estimated assessment in the amount that the Assessor considers reasonable and just.

A separate Form 632 must be filed with each assessment jurisdiction where the personal property was located on tax day. In addition to the filing of Form 5278 or Affidavit 5076, an exception to this requirement is that "Daily Rental Property" is assessed in the City or Township in Michigan where the rental store is situated, but only if certain specific requirements are met. Other exceptions include railroad company personal property and railcars owned by non-railroads, personal property used in telephone company operations (except the personal property of wireless service providers) and personal property of internet service providers. These types of personal property are assessed by the State Tax Commission.

Generally, the estimated true cash value of personal property is determined annually by applying the appropriate State Tax Commission personal property valuation multipliers to the original cost by year installed. These multipliers are shown on Form 632. The State Tax Commission strongly recommends that these valuation procedures be followed unless the Assessor has a specific reason and documentation for not using the STC approved multipliers.

The definition of "personal property" is deceptively simple. It is defined as all property that is not real property. "Real property" is defined as land and all things attached to the land on a relatively permanent basis.

Personal property may be either tangible personal property or intangible personal property. Tangible personal property is property that has a physical existence and can be used directly to fulfill a human desire or need, such as an automobile, a piece of industrial machinery, livestock or wearing apparel.

Intangible personal property is property that itself has no physical existence, other than perhaps a paper representation or electronic record of its existence. Intangible personal property merely represents an idea, right or benefit owned by the holder of the property. Examples include: stocks, bonds, bank accounts, currency and coin, architectural drawings and patent rights.

For property tax assessment purposes we are concerned only with tangible personal property. However, it should be noted that when intangible personal property is incorporated into an item of tangible personal property or real property example: when a patent right is used in the design of a piece of machinery or when architectural drawings are used in the design of a building, their contribution becomes part of the resulting real or tangible personal property.

Frequently, a facility which is clearly used as a single functional asset will exhibit characteristics which might lead one person to conclude that it is real property and

another person to conclude that it is personal property. In these cases, the Legislature has sometimes specifically directed that the facility should be treated as personal property. In other cases, the Assessor will be required to evaluate the facility to determine the correct treatment for assessment purposes.

Determining Real Property vs. Personal Property

The difficult question in determining whether property is real property or personal property comes in the area of "Fixtures." Fixtures are parts or components of real property that were originally personal property and which are capable of being detached and having an existence separate from the real property. For example, a light fixture is capable of becoming a Fixture since it can be detached, but drywall is not a Fixture since an attempt to detach it would destroy it. Not all personal property attached to real property becomes a Fixture.

The Michigan Supreme Court, in *Seacrest v Fabiano*, 274 Mich 64; 265 NW2d 488 (1936) and in a number of other cases, has approved a three-part test for determining whether attached property has become a Fixture. An item of property is a Fixture only if all of the following three requirements are met:

- The item must be attached (annexed) to the real property.
- The item must be adapted to the overall use of the real property or to the part of the real property to which it is attached.
- It must have been the objective intention of the person who attached the property to make the property a permanent accession to the real property.

An Assessor should consider a number of factors when deciding if an item of property is real property or personal property:

- Whether the property is actually or constructively attached to the real estate;
- The objective intention of the party who has affixed the property;
- Whether the item of property is a normal building component for a building of that type, or is unusual for a building of that type;
- The amount of damage to the structure which would be caused by removal of the item and how readily the damage can be repaired;
- Whether the item of property has been assessed as a part of the real property;
- Whether the item of property is used as part of the operation or process of the building occupant rather than being used to facilitate the normal use of a building of the type to which the item has been attached; and,
- Whether the item of property constitutes a personal property trade fixture installed by a tenant.

It should be noted that the value of the property does not depend on whether the item of property is deemed to be a Fixture or personal property. Assessors must ensure that they have not omitted property from assessment, or twice assessed the property, by assessing it both as a Fixture and as personal property.

Care must also be taken to make sure that a single functional asset has not been mistakenly assessed partly as a Fixture and partly as personal property. In addition to the fact that this mistake might lead to double assessment or omission of property, the mistake makes it difficult to properly analyze depreciation and obsolescence and to apply certain common valuation techniques, such as the income approach to value.

While it would be easier for Assessors if an item of property was always real property or always personal property, court decisions do not support such a consistent treatment. Assessors must follow existing legislative mandates and the guidance of the State Tax Commission in determining whether an item is real property or personal property. There are certain types of property which, by direction of statute or the State Tax Commission, must be categorized either as personal property or as a Fixture. These types of property include:

- *Trade Fixtures* are items attached to real property by a tenant, which the tenant has the right to remove at the end of the lease term and which can be detached for use elsewhere without destroying the item in question. Under Michigan Law, if the lease is silent, the tenant has the right to remove such items. They do not become Fixtures and, instead, they remain Personal Property. MCL 211.8(k) specifically provides that Trade Fixtures are assessable as Personal Property.
- *Interests in real property, the fee to which is owned by the State of Michigan or the United States* (except to the extent otherwise provided in the General Property Tax Act), which are assessable as personal property, pursuant to MCL 211.8l.
- *Mobile homes located outside licensed parks*, are assessable as real property even if not attached to the land, pursuant to MCL 211.2a.
- *Tombs and vaults located within burial grounds*, are assessed as personal property, pursuant to MCL 211.7(t).
- All property of *gas and coke companies, natural gas companies, electric light companies, waterworks companies, hydraulic companies, and pipe line companies transporting oil or gas as public or common carriers, including rights-of-way and the easements* or other interests in real property, are assessed as personal property, pursuant to MCL 211.8(g).
- *Underground rock strata* used for gas storage purposes when leased or owned separately from the surface, are assessed as personal property, pursuant to MCL 211.8(g), if the owner of the interest does not own the surface.
- The *track, roads, or bridges of street railroad, plank road, cable or electric railroad or transportation companies, bridge companies, and all other companies not required to pay a specific tax*, are assessed as personal property pursuant to MCL 211.8(g).
- During the tenancy of the Lessee, *leasehold improvements* and structures installed on the real property by the Lessee, to the extent that the improvements add to the value of the real property and are not included in the assessment of the real property, which may be assessed as personal property, pursuant to MCL 211.8(h). (Notice that unless the lease existed before 1984 and has not been substantially

renegotiated since, these improvements may, in the alternative, be assessed to the real property interest of the landlord.)

- A *sub-leasehold estate* to the extent that the excess rentals are not attributable to leasehold improvements, are assessed as personal property, pursuant to MCL 211.8(i).
- To the extent not assessed as real property, the *value of a leasehold estate* created by the difference between the income that would be received by the Lessor from the Lessee on the basis of present economic income minus the actual rent, except in cases where the lease has not been renegotiated after December 31, 1983, is assessed as personal property, pursuant to MCL 211.8(j).
- *Wind energy systems*, are assessed as personal property, pursuant to MCL 211.8(l).
- Solar energy systems are assessed as personal property pursuant to STC determination.
- After December 31, 2002, *buildings and improvements located on leased real property*, are assessed with a **separate** real property assessment, as described in STC Bulletin 8 of 2002 and Bulletin 1 of 2003, if the value is not otherwise included in the assessment of the real property. It should be noted that this provision results in tenant-owned structures such as communications towers being assessed as real property rather than as Personal Property.
- *Freestanding signs and billboards*, are assessed as personal property, pursuant to MCL 211.34c.
- *Methane digesters and methane digester electric generating systems, biogas gasification systems and thermal depolymerization systems* are implicitly deemed to be personal property, pursuant to MCL 211.9(j), but are implicitly not exempt unless specific statutory qualifications are met.
- *Removable Docks*, the State Tax Commission has determined that removable docks are real property Fixtures, even if they are removed on a seasonal basis and/or are floating docks. The Commission has noted that even a floating dock must be attached to the shore or it will float away. Because the dock is attached to the upland, it is adapted to the overall use of the property (recreational or commercial) and since the dock is placed pursuant to a permit that is tied to the particular parcel of land, it is intended to be permanent.
- *Industrial Process Piping and Process Power*: Typically, electric power lines and piping associated with an industrial building which is being valued on the real property roll are part of the real property. Individual pieces of equipment, such as, process electric power and piping “drops,” are an installation cost for the equipment and therefore personal property. However, this distinction is often easier to state than it is to implement. Particularly in cases where the industrial plant is engaged in a continuous process such as chemical manufacturing, industrial gas manufacturing, integrated steel making, etc., that requires special purpose (single use) real property. It is often difficult in these situations to determine where the real property ends and the personal property begins.
- *Appliances at Multiple Residences and Apartment Buildings*: There is significant difference among assessment jurisdictions in the treatment of appliances which are not built-in, but which are included with the rental of a multiple residence or

apartment building units. Many assessment jurisdictions value multiple residences and apartments using the income approach and often treat appliances as real property and do not include them in the personal property assessment. Some jurisdictions, which rely on the income approach, still separately assess appliances as personal property by allocating the overall indication of value from the income approach between the personal property and the real property.

Leasehold Improvements

“Leasehold improvements” are land improvements made by a tenant or improvements made by a tenant to a structure which was erected and/or which is owned by the landlord. A taxpayer is required to report all leasehold improvement expenditures in Section M on Page 4 of the Statement, even if the taxpayer believes the improvements add no value to the real estate.

Beginning in 2017, the State Tax Commission is directing assessor to assess all leasehold improvements to the real property and not as personal property. It is critical that these improvements are not assessed twice.

“Trade fixtures” should not be reported as leasehold improvements. As discussed earlier, a “trade fixture” is property which was acquired by a tenant as detached personal property but which has been attached to leased or rented real property by the tenant and is capable of being detached again for use elsewhere. It is common for taxpayers to classify certain trade fixtures, such as telephone systems, signs, security systems, etc., as leasehold improvements in their financial accounting records, but the General Property Tax Act provides that trade fixtures are personal property and are assessable to the tenant.

The State Tax Commission recommends that such tenant improvements be assessed as part of the real property. However, the STC also recognizes that unless the real property lease is a pre-1984 lease, the Assessor has discretion to assess the improvements to the tenant on the personal property roll or to the landlord on the real property roll.

Use of Approved Personal Property Statements

MCL 211.19 indicates:

“Sec. 19. The written statement under oath, provided for ... shall be in such form and of such content as may be prescribed by the state tax commission”

Assessors must either use the current STC approved Statement or an alternate form of the Statement approved by the STC. If an Assessor wishes to use an alternate Statement, it must be submitted to the STC for approval each year.

The STC requires that all approved Statements contain the following sentence in the lower right hand corner of the first page of the form: "Form Approved by the State Tax Commission on (date) ." This makes it clear to Assessors and taxpayers that the form has received STC approval. Sometimes an Assessor may have reason to believe that a particular Statement should not be followed. MCL 211.24 states that the Assessor is not bound to follow these Statements but should exercise his or her best judgment.

Both real and personal property statements received by Assessors are confidential and should not be made available for public inspection and are not subject to release under the Freedom of Information Act. MCL 211.23 states in part that "... no such statement shall be used for any other purpose except the making of an assessment for taxes as herein provided, or for enforcing the provisions of this act, and any officer or person who shall make or allow to be made willfully or knowingly, any other or unlawful use of any such statement, shall be liable to the person making such statement for all damages resulting from such unauthorized or unlawful use of such statement."

Real and personal property statements are to be used only for the administration of the property tax at the local level, the County level, or at the State level. The Board of Review may see the Statements or working papers filed.

Assessor's Acceptance of a Personal Property Statement as Filed by the Taxpayer

The General Property Tax Act provides that an Assessor making a personal property assessment shall estimate the true cash value of all the personal property of each taxpayer and that they are not bound to follow the Statements of any person, but shall instead exercise their best judgment.

An Assessor must follow the same procedure as used in real property assessments to notify a taxpayer of their personal property assessment and a taxpayer must follow the same appeal procedures used in real property assessments. If the assessment was estimated because the taxpayer did not file a timely Statement, the taxpayer can submit the Statement directly to the March Board of Review and request that the Board revise the assessment to agree with the late filing.

The STC has jurisdiction to revise a personal property assessment that is inaccurate arising from the fact that the taxpayer filed an incorrect Statement which was used as the basis for making the assessment (an incorrect report). The Commission has jurisdiction to adjust the assessment for the year in which the petition is received and for the two immediately preceding assessment years. This petition is filed using Form L-4155 (Form 628).

Personal property which is constructed by the taxpayer, or which is constructed by a contractor under the direction of the taxpayer, must be reported on the Statement at the cost that it would have been paid to acquire the same property if the taxpayer had purchased it already constructed and installed in the normal course of retail trade, even if the cost entered on the taxpayer's accounting records is different.

Personal Property Statement Reporting Issues

Assessors will normally compare prior year's Statements with the current years report to ensure taxpayers are not "shopping" for a faster depreciation table. This comparison will also ensure that values do not disappear from a Statement without explanation.

Restatement of Personal Property Costs: The State Tax Commission's recommended valuation procedures are designed for use in conjunction with cost new and acquisition year new. The continued reporting of cost new and acquisition year new permits uniform treatment of taxpayers who own similar personal property and allows the Assessor to use the State Tax Commission's recommended valuation procedures rather than appraising the property each year.

The instructions to the Statement require the taxpayer reports the cost new and acquisition year new of the personal property, even if the taxpayer acquired the property in a year later than the year it was originally placed in service and/or at a cost different than the cost of the personal property when it was new. If the cost new and acquisition year new are not known and cannot be reasonably determined, the instructions provide alternative reporting requirements that are designed to provide the Assessor with sufficient information to value the property.

The responsibility for correct reporting rests with the taxpayer. Most questions regarding correct categorization of items of personal property on the Statement can be addressed by the instructions on the Statement or by STC Bulletin 12 of 1999, Bulletin 1 of 2000 and Bulletin 3 of 2000. The taxpayer is not permitted to independently determine the correct reporting of items which are not listed in the instructions to the Statement. The categorization of personal property reported on Page 2 of the Statement depends on the nature of the property itself and is not based on the use of the personal property. For example, a motorized conveyor used as part of a testing process is reported as an item of machinery and equipment, in Section B of the Statement, not as an item of electronic test equipment reported in Section D of the Statement.

Sales Tax, Freight, and Installation: Original costs are required to be reported on the Statement by year installed and should include the cost of sales tax, the cost of freight, and the cost of installation. Sales tax must be included even if it was not paid.

Fully Depreciated Assets: The cost of fully depreciated assets which are still in an owner's possession should continue to be reported on the Statement by year of acquisition.

Expensing Policy: An owner should report all assessable personal property to the Assessor regardless of the owner's policy of expensing those acquisitions which are less than a certain dollar amount for federal income tax purposes. Items such as grocery carts, pallets, parts racks, small tools, hand tools, bakery pans, etc., are assessable as personal property even though they may be expensed for income tax purposes.

Certain items such as hand tools may be expensed because they are constantly being broken or lost and often do not last a whole year. These items are assessable and the Assessor should estimate how many were on hand on tax day and determine a reasonable method for valuing them.

Repair Expense vs. Capital Expenditure: An expenditure on existing plant assets can be either an expense or a capital expenditure. It is an expense if it only helps to generate current revenues rather than future periods' revenues, e.g., lubricating a machine, replacing a fan belt.

It is a capital expenditure if it benefits future periods' revenues either by increasing the quality of services obtained from the asset or extending the quantity of services, i.e., the life of the machine.

The cost of capital expenditures should be reported on the Statement. It may also be necessary to adjust the original acquisition cost of an asset when capital expenditures are made on it. Example: if 25% of a machine acquired in 1975 is rebuilt in 1991, 25% should be deducted from the 1975 acquisition cost.

Although taxpayers sometimes assert that certain expenditures which have been booked on fixed asset schedules as capital expenditures were mistakenly capitalized rather than expensed, the STC recommends that assessors require a taxpayer to report its capital expenditures incurred to recondition or rebuild an item of personal property and to reflect the retirement of components, using the same methodology as was actually used for financial accounting purposes.

Section 179 Property, Section 38 Property or other Federal Tax Investment Tax Credit Programs: The total original cost of personal property should be reflected on the Statement by taxpayers even though a portion of the cost may have been recorded in the taxpayers' accounting records as an expense under Section 179 of the Internal Revenue Code or under another Federal Tax Investment Tax Credit program. Under these programs a taxpayer is permitted to treat the cost of qualifying property as an expense rather than a capital expenditure. However, for personal property assessment purposes the full acquisition cost should be reported prior to any reductions for investment tax credits.

Standby Equipment: Standby equipment is equipment which is not usually in use but is ready and immediately on hand for use when needed. For example, a company might have a standby boiler which is used when there are problems with the main boiler. This could also be true of production machinery and equipment standing by for use in

emergencies. Standby equipment is considered necessary for production even though it is not being used during certain periods of time. Standby equipment is valued the same as machinery and equipment in use. Personal property used on a seasonal basis and not actually used on or around tax day, does not affect the obligation to report the property as being in-service.

Buildings and structures on Leased Land: Pursuant to P.A. 415 of 2000, buildings and other structures placed by a tenant or non-owner on leased or non-owned land are assessed on the real property roll, by establishing a separate real property assessment. The exception to this is that freestanding signs and billboards are assessed as personal property.

Construction-in-Progress: All machinery and tools being installed or constructed on tax day should be reported to the Assessor at 100% of the costs incurred as of that day. The Assessor should then deduct a Construction-in-Progress allowance of 50% to arrive at the true cash value estimate.

In Michigan, the concept of "Construction in Progress" closely corresponds to the methodology used in financial accounting to record items of personal property in the taxpayer's fixed asset records. On the tax day when construction is complete, the total costs including freight, installation and sales tax must then be reported in the year of completion even though they were incurred over several years. The year of completion becomes the year of purchase for depreciation purposes.

If an asset (including a self-constructed asset) is in the assessment jurisdiction on tax day but is under construction or has not otherwise been placed in service, it is reported as "Construction in Progress" on Line 14 of the Summary and Certification Section on Page 1 of the Statement. For purposes of reporting "Construction in Progress," only the expenditure incurred relating to the portion of a project that will be reported as personal property when the asset is placed in service should be reported as "Construction in Progress" on the Statement.

Leased Equipment: MCL 211.9c states that inventory is exempt, but it also goes on to state that "Inventory does not include personal property under lease or principally intended for lease rather than sale." Therefore, personal property leased or principally intended for lease is not exempt as inventory. Examples of this type of equipment include rental clothing, rental uniforms, rental linen, rental tools, rental computers, rental copiers, rental office machines, rental furniture, rental video cassette recorders and rental video cassettes. Also included are those items in an equipment dealer's hands which are more than very occasionally rented rather than sold.

Leased equipment should be reported at selling price new so that all equipment is valued the same whether it is purchased or leased. The reported selling price new must include sales tax, freight and installation, even if those costs were incurred by the Lessee. The Assessor will then apply the original cost multipliers to the selling price new to obtain an estimate of true cash value.

Sometimes a manufacturer of equipment will exclusively lease equipment rather than sell it. In this situation, the Assessor must estimate what the selling price would be. One or more of the following methods may be used to estimate selling price new:

- Capitalization of lease income;
- Comparison to similar equipment which has sold; or
- Manufacturer's cost adjusted to selling price new. This approach is sometimes unreliable because a company may or may not include in their manufacturer's cost the cost of management, research, engineering, promotion, advertising, overhead, transportation and installation. Other items of indirect cost may or may not be ascribed to particular products.

Leased equipment should be assessed to the owner (Lessor) of the equipment regardless of clauses in the lease which state that the Lessee is responsible for taxes. These clauses are a private matter between the Lessor and Lessee and do not affect to whom the property is assessed. If the owner is not known, the property should be assessed to the person in possession. However, see also Bulletin #2 of 1992 regarding certain bank-owned personal property.

Leased equipment is reported by the Lessee, for informational purposes only, in Section J on Page 3 of the Statement. The Lessee should not report leased equipment along with its owned personal property unless the Lessor is a bank, savings and loan or credit union or unless the property has in Industrial Facilities Exemption. This is true even if the lease arrangement is treated as a capital lease under GAAP and/or for federal income tax purposes, or is a lease arrangement of the type sometimes referred to as a "conditional sale." If the leased personal property is "qualified personal property" of a "qualified business" it is reported in Section I.

Lessees often purchase equipment at the end of a lease. Care should be taken to assure that equipment is properly reported at the acquisition cost new and acquisition year new after ownership transfers.

The State Tax Commission has directed that a leasing company must include or impute sales tax, freight and installation costs as part of its reported cost, even if the cost was incurred by the Lessee rather than the Lessor, and even if an election was made to pay periodic use tax on the lease payments rather than sales tax. However, if the Lessee is exempt from sales and use tax, then such taxes should not be imputed.

Personal Property Discovery

The Assessor is responsible for the valuation of all assessable personal property in their jurisdiction. This involves the discovery of the location of all assessable personal property on tax day and a determination of its value. A formalized approach to this discovery process usually produces the best results.

First, begin the discovery process by becoming thoroughly familiar with the prior year's personal property assessment roll and filed Statements. The following are changes which occur during the year and may affect the following year's assessment roll.

- December or July Board of Review changes made to correct clerical errors or mutual mistakes of facts. (See MCL 211.53b.)
- Michigan Tax Tribunal changes made to correct clerical errors or mutual mistakes of fact or any other Michigan Tax Tribunal change. (See MCL 211.53a.)
- State Tax Commission changes made as a result of the fact that property liable to taxation has been incorrectly reported or omitted. (See MCL 211.154.)
- New business firms entering the assessing jurisdiction.
- Old business firms leaving the assessing jurisdiction.
- Other reasons for changes may be found.

Second, after securing whatever information is available through sources which are available without leaving the office, the Assessor must conduct an annual personal property canvass of the assessing jurisdiction. This is a *very important procedure*. The proper method for conducting a personal property canvass is discussed below.

Third, following the annual canvass, questionnaires can be sent to those property owners with whom the Assessor was unable to consult in order to obtain information about ownership, leased equipment, exemptions being claimed, etc.

Fourth, annual, or periodic, inquiries should be made of all exempt organizations to determine whether the organizations had in their possession, on tax day, personal property owned by others. It is quite common for exempt organizations to lease equipment rather than purchase it. This equipment owned by others is assessable to the owners of the equipment. The following are some of the exempt organizations which may have assessable leased equipment: hospitals, clinics, public and private schools, colleges and universities, banks, savings and loans, credit unions, federal, state, and local government offices.

The Personal Property Canvass

The personal property canvass involves visiting every address, firm, location or place where assessable personal property may be found. The objectives of the canvass are to gather all the relevant information necessary to prepare accurate assessment rolls, to promote uniformity within classes of property and equitable assessments between the same or similar taxpayers, and to cost-effectively collect the maximum revenue allowed by law.

During the canvass, the Assessor should visit new businesses in the community and gather necessary information about ownership of the businesses, correct mailing addresses and what the likely reported costs will be. The Assessor can note changes which have occurred in existing businesses since the filing of the previous year's Statements. With the previous year's Statement or true cash values in hand, the

Assessor can also make judgments about whether those Statements were properly filed and whether an audit of a company's books and records is necessary. Business owners can also be questioned about the ownership of leased equipment located at the premises so that statements can be sent to the owners of leased equipment. The personal property canvass can also be a valuable public relations tool which can set the tone of the relationship with the business owner for many years to come.

One good procedure is to deliver the Statement during the canvass and record who received it and the date delivered. A written record of the personal property canvass should be maintained.

The timing of the personal property canvass is very important. Usually, the month preceding and following tax day, December 31, are considered good times. Because personal property is often moved from one assessment jurisdiction to another, the canvass should be conducted as close to tax day as possible. Many assessors conduct canvass on tax day itself to search for such personal property. Of special concern in many jurisdictions is the contractor's equipment canvass whose purpose is to discover mobile construction machinery and equipment and other personal property items which are located in a taxing jurisdiction on tax day. Such equipment is frequently found at building sites, demolition areas, contractors' yards, etc. Types of equipment to be listed include cranes, bulldozers, tractors, unlicensed trailers, welders, compressors, forms, etc.

The General Property Tax Act includes the following sections that establish the legal authority to perform audits of Statements.

MCL 211.21. Willful Neglect to Make Statement, Penalty; Complaint

Sec. 21. In every case when any person or member or any firm or officer of any corporation shall willfully neglect or refuse to make out and deliver a true and correct sworn statement, under oath, administered by the supervisor or other assessing officer or members of the board of state tax commissioners herein provided for or other officers shall answer falsely or refuse to answer questions concerning his property or property under his control, as required by this act, such person shall be deemed guilty of a misdemeanor, and upon conviction thereof shall be punished by imprisonment in the county jail not less than 30 days nor more than 6 months, or by fine not less than 100 dollars nor more than 1,000 dollars, or by both such fine and imprisonment in the discretion of the court. And it shall be the duty of the supervisor, assessing officer, and each member of the board of state tax commissioners whenever he is satisfied that any person liable to make such assessing statement is justly liable to such penalty, to report the case to the prosecuting attorney of the county and make proper complaint for such prosecution.

MCL 211.22. Incorrect or Absent Statement; Testimony Assessment

Sec. 22 If the supervisor or assessing officer, a member of the state tax commission, or the director or deputy director of the county tax or equalization department shall be satisfied that any property statement or affidavit made is incorrect, or if, by reason of absence or other cause, said sworn statement cannot be obtained from the person, firm or corporation whose property is so assessed, the supervisor, assessing officer, any members of the state tax commission, or the director or deputy director of the county tax or equalization department may examine, on oath, to be administered by any of them, any other person or persons whom he or she may have good reason to believe and does believe has knowledge of the amount or value of any property owned, held, or controlled by such person so neglecting or refusing or omitting to be examined or to furnish such statement, and such supervisor or assessing officer is authorized to set down and assess to such person, firm or corporation so entitled to be assessed, such amount of real and personal property as he or she may deem reasonable and just.

MCL 211.22a. Personal Property Examiners; Certification; Examination of Property

Sec. 22a(1) The state tax commission, upon presentation by representatives of county tax or equalization departments, townships and cities, of satisfactory evidence of education, experience, or by passage of a test conducted by the commission, shall certify a successful applicant as a qualified personal property examiner. A certified personal property examiner may examine only the property or the cost records relating to such property of any corporation, firm, or individual liable to assessment within their county, township or city for property taxes under this act.

(2) Upon written request of a city, village or township assessing officer to examine the property or books of any corporation, firm, or individual, a certified personal property examiner of the county tax or equalization department shall conduct the examination. Where there is no certified personal property examiner in the county equalization department, the examination shall be made by a representative of the state tax commission at the expense of the city, village or township.

(3) Where any corporation, firm or individual is subject to personal property assessment in more than 3 counties of the state then the corporation, firm or individual may request an examination be made at their expense by a representative of the state tax commission at a rate of 1/10 of 1 mill of the gross value of the personal property of said corporation, firm or individual under examination.

Beginning in 2019, all certified assessors (MCAO, MAAO and MMAO) will receive a Personal Property Examiner endorsement as part of their regular certification and will no longer need a separate PPE Certification.

Jeopardy Assessment (P.A. 55 of 1956)

MCL 211.691 authorizes the jeopardy assessment of personal property taxes. The treasurer of any Township, City, or Village is authorized to accelerate the date on which any personal property tax would otherwise be due provided the treasurer has good reason to believe one of the following:

- The taxpayer has fled or is about to flee from the State or that they are concealed therein, thereby tending to jeopardize the collectability of any personal property tax assessed and levied by the regular assessment and collection procedure; or
- The Taxpayer has assigned, disposed of or concealed, or is about to assign, dispose of or conceal any of this property, thereby tending to jeopardize the collectability of any personal property tax assessed and levied by the regular assessment and collection procedures; or
- The Taxpayer has removed or is about to remove any of his property out of this state thereby tending to jeopardize the collectability of any personal property tax assessed and levied by the regular assessment and collection procedure; or
- Other facts exist, as specified specifically by the treasurer, which tend to jeopardize the collectability of any personal property tax assessed and levied by the regular assessment and collection procedure.

Personal Property Exemptions

Licensed Vehicles, Aircraft, and Watercraft: MCL 257.801 states that the “secretary of state shall collect taxes at the time of registering a vehicle, which shall exempt the vehicle from all other taxation, either state or local.” Motor vehicles and trailers which have been registered with the Michigan Secretary of State by paying the fee provided in Section 801 of the Motor Vehicle Code, MCL 257.801, are exempt from payment of all other taxes, including personal property taxes. Vehicles and trailers which have not paid the fee provided in Section 801, including vehicles kept in Michigan but not registered on tax day, are not exempt. A vehicle which is engaged in interstate commerce and which has paid a pro rata portion of the registration fee provided in Section 801 is deemed to be registered for purposes of the exemption contained in that section.

Owners of large parcels of land may have unlicensed vehicles for use only on their own property and certain taxpayers own vehicles, particularly tractor trailers, which are kept in Michigan but registered in other states, without apportionment of the registration fee to Michigan based on fleet mileage. These vehicles are assessable.

“Special mobile equipment,” for which a voluntary fee is paid pursuant to Section 802 of the motor vehicle code, is not exempt. The permit issued upon payment of that voluntary fee is not a vehicle registration under Section 801 and, therefore, it does not serve to exempt the vehicle. “Special mobile equipment,” which is defined as a “vehicle not designed or used primarily for the transportation of persons or property and incidentally operated or moved over the highways, including farm tractors, road construction or maintenance machinery, mobile office trailers, mobile tool shed trailers,

mobile trailer units used for housing stationary construction equipment, ditch-digging apparatus, and well-boring and well-servicing apparatus,” is not exempt from personal property taxation.

A watercraft for which a fee has been paid subject to the provisions of MCL 281.1033 is exempt from all property taxes. Coast Guard documentation is not a substitute for registration of the watercraft with the State of Michigan and the if the watercraft is not properly registered with the State, it is subject to property tax assessment.

Aircraft registered under the provisions of MCL 259.77 are exempt from all property taxes. Further certain aircraft and their spare parts (“rotables”) which are exempt from registration pursuant to MCL 259.76 are also exempt from property tax assessment, pursuant to MCL 211.9(1)(t).

An assessable watercraft or aircraft or the equipment located thereon presents unusual valuation issues and must be reported in Section G of the Personal Property Statement, Form L-4175 (Treasury Form 632).

Inventory: Inventory, as defined by the General Property Tax Act, MCL 211.9c, is exempt from assessment. The statutory definition of exempt inventory includes:

- Stock of goods held for sale or resale in the regular course of wholesale or retail trade;
- The finished goods, goods in process and raw materials of a manufacturing business;
- Supplies which will be consumed during the current period; and
- Heavy earth moving equipment being held for retail sale, which can continue as exempt inventory for a limited time despite the fact that the merchant is actively renting the equipment under prescribed circumstances.

Inventory does not include personal property under lease, or principally intended for lease rather than sale (except for heavy earth moving equipment owned by a retail vendor which is held for sale but which is rented or leased under permitted circumstances for a limited time) or personal property allowed a deduction or allowance for depreciation or depletion under the Internal Revenue Code of 1986 (even if the deduction or allowance is not taken).

Contrary to the impression held by some, there is no exemption of heavy earth moving equipment. However, the provision in the General Property Tax Act permits heavy earth moving equipment to continue to be treated as the exempt inventory of a merchant, despite the fact that the merchant is actively renting the equipment under specified circumstances. If the owner of the heavy earth moving equipment is not holding the equipment for sale in the regular course of retail trade (if the owner is not a dealer), then the equipment is assessable. Further, even a dealer must qualify such equipment for continued treatment as inventory by completing and filing Form 3711 and by adhering to record keeping and other requirements which are detailed in the instructions to Form 3711 and in State Tax Commission Bulletin 4 of 2001.

MCL 211.9c(3) states in part: "Inventory does not include property allowed a deduction or allowance for depreciation or depletion under the federal internal revenue code." In applying this statutory provision, the question is whether the property qualifies for the depreciation or depletion allowance, not whether a particular taxpayer actually claims such allowances. Since items which are allowed a deduction or allowance for depreciation or depletion are not inventory, they are assessable as personal property. An example of property in this category is nuclear fuel. Ordinarily fuel is exempt as inventory but the Internal Revenue Code allows nuclear fuel to be depreciated, and therefore, it is assessable as personal property. Where repair parts are allowed a depreciation allowance (such as when they are held as standby equipment), they are also assessable as personal property.

However, the Assessor should note that the law does *not* state that just because personal property is expensed by an accounting system that it is exempt as inventory. On the contrary, frequently, accounting systems will call for certain items to be expensed but they are still assessable as personal property.

Exempt Special Tools—Dies, Jigs, Fixtures, Molds, Patterns and Special Gauges: A "special tool," as defined in the MCL 211.9b is exempt from personal property taxation. A "special tool" is a finished or unfinished device such as a die, jig, fixture, mold, pattern, special gauge or similar device that is used or is being prepared to be used, to manufacture a product and that cannot, without substantial modification, be used to manufacture another product. A "product" is a part, a component, a sub-assembly, a special tool or completed goods that are available for sale or lease in wholesale or retail trade.

The definition of "special tool" does not encompass or include devices that differ in character from a die, jig, fixture, mold, pattern, special gauge and specifically does not include machinery and equipment even if customized to make one product and even when used in conjunction with "special tools." A die, jig, fixture, mold, pattern or special gauge or similar device which does not meet the definition of a "special tool" is designated as a "standard tool" and is reported in Section H, of the Statement. However, "standard tools" are rare, arising from the fact that a die, jig, fixture, mold, pattern, special gauge or similar device, due to its nature, typically cannot make more than one product, absent substantial modification. Equipment which measures or which holds items together or in place, but which is adaptable to many uses, such as a micrometer, a tape measure or a common clamp, is neither a "special tool" nor a "standard tool" and is reported as equipment in Section B of the Statement.

Air Pollution Control Facilities and Water Pollution Control Facilities: MCL 336.1, provides for the exemption of air pollution control facilities, both real and personal property, when covered by a certificate issued by the State Tax Commission. Similarly MCL 323.351 provides for the exemption of water pollution control facilities, both real and personal property, when covered by a certificate issued by the State Tax Commission.

L.P. Gas Containers: Act No. 317 of Public Acts of 1990 provides for the following exemption:

“Sec. 9. The following personal property is exempt from taxation:

... (r) Liquefied petroleum gas tanks located on residential or agricultural property and used to store liquefied petroleum gas for residential or agricultural property use. As used in this subdivision, ‘liquefied petroleum gas’ means that term as defined in section 51 of Act No. 150 of the Public Acts of 1927, being section 207.151 of the Michigan Compiled Laws.”

Liquid Propane Gas (LPG) tanks located on residential or agricultural property for residential or agricultural use are exempt for the 1991 and subsequent tax years. LPG tanks used for commercial or industrial use remain taxable. Bulk LPG storage facilities and customer tanks located at the bulk storage facility on Tax Day are assessable. Further, bulk storage tanks over 2000 gallons are typically assessed as real property improvements, rather than as personal property. See the discussion of such facilities in the instructions to Section G of the Statement.

Financial Institutions: Personal property owned by a state bank or trust company, a national banking association, an incorporated bank holding company, a savings and loan association or a credit union is exempt from taxation (MCL 211.9(m), MCL 489.858(1), and MCL 490.105.) However, this exemption does not extend to non-banking subsidiaries of such financial institutions that are separate legal entities from the bank and do not pay state franchise fees, or to the real property interests of the financial institutions. Buildings, or structures (such as kiosks) on leased land and leasehold improvements, are not exempt. Further, personal property owned by such entities which is made available to a business conducted for profit (a “for-profit” user), such as a Lessee, or which is made available to its own non-banking subsidiary, is not exempt (MCL 211.9(m), MCL 487.14309 and MCL 487.3416). State Tax Commission Bulletin 2 of 1992 provides that an exempt financial institution must file an information return, on a form approved by the STC in each assessment jurisdiction where it has personal property being used by a “for-profit user.” This return must disclose the name and address of the “for-profit” user, the acquisition cost of the personal property in question and the year of acquisition of the property.

The courts have ruled in *Michigan National Bank v City of Lansing* (MTT #28884-28888, 28890; Michigan Court of Appeals #44162-44167; Michigan Supreme Court #65050-65055) that night depository boxes, drive-in windows, remote transaction units, and vault doors are real property when annexed to a building and/or land used as a banking facility and are, therefore, not entitled to exemption regardless of who owns the land and/or building. The vault and the alarm system are also generally considered to be real property. Safe deposit boxes and business machines are deemed to be personal property.

Automated teller machines are considered to be personal property regardless of whether they are free-standing units or are installed in a wall. Automated teller machines are, therefore, exempt from taxation when owned by a financial institution. Sometimes, however, automated teller machines are leased by the financial institution and are then typically assessable.

Pursuant to MCL 211.19, a bank can be required to complete a general Statement and must always report its leasehold improvements which it has made available to its non-bank subsidiaries and any personal property which it is leasing from a Lessor.

Agricultural Property: MCL 211.9(j) states in part that personal property "... actually being used in agricultural operations ..." is exempt from taxation. Attorney General Opinion #6204 states that this "... exemption is not predicated upon ownership of personal property by an entity engaged in agricultural operations...." Therefore, fertilizer equipment leased to a farmer was considered to be exempt even though not owned by the farmer.

The General Property Tax Act provides that personal property actually used in agricultural operations is exempt. Equipment attached to specialized agricultural structures, such as livestock feed systems integrated into the building, may be deemed to be part of the real property and may not qualify for exemption. The exemption for agricultural personal property does not require that the property must be owned by, or even used by, a farmer. Instead, the exemption depends on the use to which the property is actually being put. The personal property of a contractor, when providing services that are part of agricultural operations, such as combine or fertilizing services and the personal property of leasing companies, where the property is actually used exclusively in agricultural operations, may qualify for exemption. Generally, the property must be used directly and exclusively in agricultural operations. Personal property used in retail sales and in food processing does not generally qualify for exemption.

The statute defines property actually used in agricultural operations as: "farming in all its branches, including cultivation of the soil, growing and harvesting of an agricultural, horticultural, or floricultural commodity, dairying, raising of livestock, bees, fur-bearing animals, or poultry, turf and tree farming, raising and harvesting of fish, collecting, evaporating, and preparing maple syrup if the owner of the property has \$25,000.00 or less in annual gross wholesale sales, and any practices performed by a farmer or on a farm as an incident to, or in conjunction with, farming operations, but excluding retail sales and food processing operations".

The exemption does extend to equipment used in a manner incidental to the farming operation that prepares the crop for market and does not substantially alter the form, shape, or substance of the crop, if not less than 33% of the volume of the crops processed in at least three of the last five years were grown by the Michigan farmer who is the owner or user of the processing equipment.

Methane digesters and methane digester electric generating systems, biogas gasification systems and thermal depolymerization systems must meet conditions set in the statute to be exempt.

Interstate and Foreign Commerce: The Constitution of the United States specially prohibits the taxation of certain products in interstate and foreign commerce. Article 1, Section 8, Clause III reads: "The Congress has power to regulate commerce with foreign nations and between the several states."

As long as merchandise retains the character of an import, it is exempt from taxation by the state unless there is consent from Congress. The Michigan Court of Appeals in *Thyssen Steel Corp. v State Tax Commission*, 38 Mich App 363 (1972) states that "... it has become well established that imports lose their constitutional immunity when the importer (1) sells them, or (2) 'breaks up the packages' or (3) puts them to the use for which they were imported." Consult the State Tax Commission when dealing with transportation equipment involved in interstate or foreign commerce.

Exempt Personal Property Used in a Business Conducted for Profit: MCL 211.14(5) states in part that "... personal property not otherwise taxed under this act which is in the possession of any person, firm or corporation using same in connection with a business conducted for profit shall be deemed the property of such person for taxation and assessed to him accordingly." This language authorizes the imposition of a tax upon the right to use another's tax exempt personal property.

Householder Exemptions: MCL 211.9(k) states that the following personal property is exempt from taxation: "Personal property to the state equalized value of not more than \$500.00 used by a householder in the operation of a business in the householder's dwelling or at one other location in the city, township, or village where the householder resides." This exemption does not apply to personal property owned by a corporation or a partnership.

Although the General Property Tax Act provides that personal property owned and used by a householder, such as customary furniture, fixtures, provisions, fuel, wearing apparel, personal jewelry, family pictures and books are exempt from personal property taxation, such personal property is not exempt if it is used to produce income or if it is held for purposes of speculative investment.

Computer Software: Generally, software is exempt from property tax assessment, pursuant to MCL 211.9d. However, there are two exceptions, both relating to instances where it would be difficult to identify the portion of an acquisition cost that was the cost of acquiring software and the portion of the acquisition cost that was the cost of hardware.

The first exception is that software is assessable if it is incorporated as a permanent component in hardware and is not commonly available for purchase separately.

The second exception is that software is assessable if it is purchased in the same transaction as the hardware with which it is used, unless the separate cost of the software is commemorated at the time of acquisition, both by a separate invoice or invoice amount and by the assignment of a separate line entry in the fixed asset records developed for financial accounting purposes.

The phrase “and assessable software,” as contained in the instructions to Section F of the Statement, does not imply that most or all software is assessable. Instead, the phrase simply indicates that software of the type designated in the two exceptions to exempt status, as described above, must be reported in Section F. Essentially, the cost of these types of software cannot first be imputed, or estimated, and then removed from the reported cost of related hardware. It should be noted that software that is incorporated into or used with hardware that is not reported in Section F of the Statement is reported in the same section of the Statement as the hardware into which it is incorporated or is used with.

Chapter 10 Board of Review

The Board of Review (BOR) was created by the General Property Tax Act, Section 211.28. The Board of Review has three statutory functions:

1. The BOR meets in March to examine the current assessment roll to determine if the assessor has assessed all property liable to taxation and to correct errors on the names of taxpayers, legal descriptions, assessments, classifications, and valuations.
2. The BOR serves as an appeal board hearing protests from property owners or their agents regarding the assessment established by the assessor. It may adjust assessments it deems unfair. It can add property to the roll that has been missed and hears appeals of denials by the local assessor of continuation of agricultural exemptions. It can grant or deny exemptions of homestead and agricultural property for homeowners who owned and occupied a homestead on June 1 or whose property qualified as agricultural property on May 1 and the exemption was not on the roll.
3. The BOR may meet in July and December to accept and approve the correction of clerical errors, mutual mistakes of fact or certain qualified errors that are discovered after the taxpayer receives the tax bill. They may also hear denials of new qualified agricultural appeals. Finally, they may also grant poverty exemptions at the July and December meetings.

The General Property Tax Act creates a board of local citizens to examine and review the assessments and correct errors in the names, descriptions, and assessments. They also hear taxpayer protests of their assessment. The BOR has limited power to grant homestead and qualified agricultural property exemptions, and to grant Poverty exemptions.

Members of the BOR must be electors of the Township. An elector must be 18 years old, a U.S. citizen, and have lived at least 30 days in the Township where they will serve. Two-thirds of the Board must be property owners. The Township Board appoints the BOR members to two-year terms beginning on January 1 of each odd numbered year.

Township Board members are not eligible to serve on the BOR. The spouse, mother, father, sister, brother, son, daughter or adopted child of the assessor is also prohibited from serving on the Board.

The Board of Review consists of three persons. The Board may be expanded to six or nine persons. If six or nine persons are appointed, they must divide into committees of three for purposes of hearing and deciding appeals. The full Board must meet in general session to review the roll. A majority of members constitutes a quorum. If sub-committees are created, each committee will decide only those appeals it heard.

The Township may appoint not more than 2 alternate members for the same term as regular members of the board of review. Each alternate member must meet the same requirements of a regular member including eligibility and oath of office. An alternate member may be called to perform the duties of a regular member of the board of review in the absence of a regular member. An alternate member may also be called to perform the duties of a regular member of the board of review for the purpose of reaching a decision in issues protested in which a regular member has abstained for reasons of conflict of interest.

The Township Supervisor is the secretary to the Board and is responsible for the minutes. If the Supervisor cannot be present, the deputy Supervisor or a Board member must perform this duty. The Township Board may appoint a clerical person to assist the Board of Review to ensure accurate minutes are taken, but the Board must still elect a secretary to oversee the clerical employee's work.

Home rule cities are required to follow the provisions of the City charter but must complete their work by the same deadline as Townships, the first Monday in April.

Terms of office begin at noon on January 1 of odd numbered years and end at noon on the next odd numbered year. The oath of office is to be taken within 10 days of appointment.

Township Boards of Review are required to meet in three separate sessions: one session to review the roll and a minimum of two sessions to hear protests from taxpayers. The BOR may have a need to hold additional sessions as necessary to hear protests. City charters establish the requirements for BOR schedules. If there is not a charter requirement, the cities follow the same schedule as Township Boards.

There are no statutory requirements for Board members. They should be citizens who are interested in public good and should be representative of the make-up of the community. They do not need to be experts in valuation of property but should be familiar with the community and have good judgment and ability to listen to both sides of an issue before making decisions. Some City charters may have specific requirements in addition to being electors of the City.

Some Board Members are compensated for serving on the Board of Review. Others are not. This is determined by City charter and statutes. Usually a per diem is paid but some units choose an hourly rate which may be more compatible with how other boards and commissions are compensated.

The BOR selects a member from each subcommittee of three to chair the meetings. Non-residents may appeal by mail. The Board may, if the governing body adopts a resolution, hear appeals by mail from local residents.

The law provides that the BOR adopt a meeting schedule, decide when decisions are to be made and if it will operate by appointments or walk-ins.

All meetings of the BOR are open meetings under the Open Meetings Act, P.A. 267 of 1976. The Open Meetings Act requires that all meetings of a public body shall be open to the public and that the meeting is held in a place available to the general public.

Under the Open Meetings Act, notices of meetings must be posted at the principal location of the Board and if appropriate at other locations determined by the governing body. If a special meeting is called, notice must be posted 18 hours in advance both at the principal office of the Board and on the website of the Board if the Board has a website at which they regularly post agenda's and minutes. (See P.A. 528 of 2012)

In addition to the requirements of the Open Meetings Act, notices of the BOR schedule must be published in three consecutive issues of the local paper or posted in five places in the local unit at least one week prior to the first meeting of the BOR.

When assessed value or tentative taxable value is increased by the assessor, a notice must be sent by first class mail to the affected taxpayer 14 days prior to the first meeting of the BOR. This notice must include the prior year's assessment, the new assessment or tentative taxable value, and the amount of change in each. Also included is the time and place of the BOR meeting.

All records of BOR proceedings are open for public inspection under the Freedom of Information Act, P.A. 442 of 1976. Records that are exempt from this act are those that include information of a personal nature. Examples would include income tax forms provided by those applying for a poverty exemption.

The first meeting of the BOR is the organizational meeting. The chairperson is elected and the rules of procedure are drafted. It is at this meeting that the Board of Review receives the assessment roll and examines it to ensure all taxable property is described

and assessed. Poverty guidelines are reviewed and generally the assessor reports on changes in laws that the Board should be aware of.

The BOR may make changes to the assessment roll but may NOT make blanket changes that affect the entire roll. If the Board makes changes, it must send a notice to the affected taxpayer. Notices may be given by mail, phone, fax, e-mail, or in person. A record should be kept of the notice and how it was sent.

The Board is not required to hear appeals at the organizational meeting but under the Open Meetings Act, must hear anyone who insists on speaking.

The second meeting of the BOR is to hear appeals from taxpayers regarding the assessments of their property. In most cases, taxpayers must appeal to the BOR before proceeding to the Michigan Tax Tribunal. The second meeting is on the second Monday in March and must begin no earlier than 9:00 a.m. and no later than 3 p.m. and last for at least six hours. There must be one additional six-hour meeting that week and there must be at least one three-hour session after 6:00 p.m.

Two members of the Board make up a quorum. If there is not a quorum, the Supervisor is to notify the members absent to attend at once or they may call upon the alternate members to serve.

A taxpayer or his/her representative may appeal to the Board. Non-residents may appeal by mail and such appeals are to be considered as if the petitioner appeared in person.

The chairperson conducts the meetings of the Board and is responsible to ensure that the meeting runs on schedule. The secretary is required to keep a record of all appeals and also which Board members were present as well as the date and time the meeting was called to order and adjourned.

Board decisions are recorded in the minutes, on the assessment roll, and on the property record card. This does not mean that the Board has authority to change the property record card.

Board of Review decisions should be based on the following criteria:

1. The assessment exceeds or falls short of the required level of assessment (50%).
2. The property is not uniformly assessed with other property in the classification.

The burden to prove an assessment is incorrect rests on the taxpayer. Utilizing the argument that "My taxes are too high" is not enough evidence to support the claim.

Boards must be completed by the first Monday in April. Notices of the decisions of the Board must be mailed by the first Monday in June and must advise the petitioner of the right to appeal to the Michigan Tax Tribunal.

The Board signs the endorsement of the final roll and the roll is turned over to the Equalization department within ten days of adjournment of the BOR or by Wednesday following the first Monday in April, whichever is first.

Poverty exemption appeals may be made to the BOR after January 1 or the year the exemption is requested. To obtain a Poverty exemption, you must: own and occupy the property as your homestead; make application to the Board of Review; supply federal and state income tax returns for all persons residing in the home or file an affidavit on the form approved by the State Tax Commission if you were not required to file a Federal or State Income Tax Return in the year in which the exemption is claimed or the immediately preceding year; and meet the federal poverty guidelines as well as the guidelines adopted by the governing body.

The Board must follow the guidelines for EVERY Poverty appeal. Failure to do so may make it difficult to defend the Board's decisions at the Michigan Tax Tribunal. Filing a poverty appeal does not prohibit filing an assessment appeal.

Poverty exemptions may be granted up to 100% and are only in effect for one year. Annual appeals must be made as the assessment is returned to previous levels the following year.

Denial of a poverty exemption may be appealed to the Michigan Tax Tribunal.

Notices of the decisions of the Board must be mailed by the first Monday in June and must advise the petitioner of the right to appeal. Valuation appeals are made to the Michigan Tax Tribunal and classification appeals are made to the State Tax Commission. Valuation appeals for properties classified Industrial Real or Personal or Commercial Real or Personal or Developmental Real do not have to appeal to the March Board of Review but can instead appeal directly to the Michigan Tax Tribunal by May 31. All other property classifications must appeal their valuations first to the March Board of Review and then to the Tax Tribunal by July 31. Classification appeals are to the Board of Review and then to the State Tax Commission by June 30.

July and December Boards of Review meet to correct clerical errors, mutual mistakes of fact or certain qualified errors. They may also hear poverty appeals not heard at the March Board of Review.

HOW TO REMEMBER THE BOARD OF REVIEW DATES (AKA – It does make sense)

The first BOR established was the March BOR. It is held on the **Tuesday following the FIRST MONDAY in March.**

The December Board of Review is to correct clerical errors, mutual mistakes of fact and qualified errors so it could not be held until the bills went out and the errors were discovered. (Tax bills used to only be sent in December.) It is held on the **Tuesday following the SECOND MONDAY in December.**

Then the laws were amended to permit the school district to collect part or all of their millage in July because their fiscal year began in the fall and it did not make sense for them to pay interest until the December collection to cover their budget. The July Board of Review is to correct clerical errors, mutual mistakes of fact and qualified errors. The July Board of Review if you are paying attention is held on the **Tuesday following the THIRD MONDAY in July.**

Chapter 11 Cost Approach

The cost approach estimates the value of a property by summing (adding) the estimated value of the land and the estimated cost (less depreciation) of the improvements. The economic principle of substitution is fundamental to the cost approach. A prudent buyer will not pay more for a property than it will cost to build a similar property.

There are two types of costs that must be considered:

1. **Reproduction cost** – cost to construct an exact duplicate of the subject.
2. **Replacement cost** – cost to construct improvement with the same functional utility of the subject.

The difference between reproduction and replacement is significant. A reproduction of a Victorian home would be very expensive due to the extensive attention to detail and the cost of craftsmen who can do the work. A replacement Victorian home would have the look and feel of the original but would be constructed of modern materials. If the subject home is fairly new, then there would not be a major difference between reproduction and replacement.

The object of the cost approach is to estimate the market value of an existing property. This requires an allowance for depreciation to the structures. The land is valued at its current market value because land cannot be reproduced.

The three principal steps in the cost approach are:

1. Valuing the land separately using market data.
2. Estimating the reproduction or replacement of the subject by building a substitute.
3. Estimating the depreciation of the subject from the time it was built to the date of the assessment.

The beginning point is to estimate cost new as of the date of the appraisal. The State Tax Commission advises that reproduction cost is generally preferred as the starting point.

The formula for the cost approach is as follows:

$$\text{Value} = \text{Land Value} + \text{Improvement Value}$$

The improved value is broken into cost new of the improvement (CN) and accrued depreciation (D) which makes the new formula: $V = LV + (CN - D)$.

Remember, depreciation is subtracted from the cost of the building **only** because land does not physically depreciate.

The first step of the cost approach is to estimate land value (discussed in Chapter 7)

The second step is to estimate cost new. The three methods of estimating cost new are:

1. The **quantity survey method** which itemizes all the materials, labor, and overhead that go into the construction of a building. It is the most accurate of all methods but is impractical for assessors due to the time involved in using this method.
2. The **unit-in-place method** where the cost of materials, labor, and overhead are combined into a single unit-in-place cost. The unit-in-place price takes into account all the separate costs and arrives at a cost per unit. The results of this method are fairly close to the quantity survey method but take less time to compute.
3. The **comparative method** is based on an average cost figure determined by dividing the total cost of a building by the area or volume of the building. Cost schedules based on volume are rarely used in residential assessing. Residential cost schedules are based on area or square foot costs. After you identify the class of the house, the story height, and the square footage of the foundation, you can find the correct cost per square foot. This number is multiplied by the area of the foundation. The Assessor's Manual has typical costs for houses of various story heights, areas, and quality. If the subject property has additional items or is missing standard features, adjustment are made for those items.

The next step in the cost approach is to estimate depreciation. Depreciation is a loss of utility and therefore of value from any cause. This loss is divided into physical depreciation (the reduction in life and value resulting from use, abuse, and the elements and begins as soon as a building is completed), functional obsolescence (the loss in value to a structure or part thereof to adequately perform the function for which it is intended), and economic obsolescence, also known as external obsolescence (a loss in value caused by factors external to the property that cause a loss in value).

Functional obsolescence is broken into curable and incurable categories. Curable functional obsolescence may be due to a deficiency or to a superadequacy. The cost to cure determines whether the item is curable or incurable. If the cost to cure is less than the added value to the structure once the item is added or removed then the obsolescence would be considered curable. If the cost to the deficiency or superadequacy exceed the value that would be added to the structure then the obsolescence is considered incurable.

Economic obsolescence is a lessening in value caused by factors external to the property. This type of obsolescence is sometimes measured by market comparisons and sometimes by rent loss. It is usually incurable and of substantial duration.

Depreciation tables for residential, agricultural, and mobile-manufactured properties are in Volume I of the Assessor's Manual. Volume II has the tables for commercial and industrial property. These tables have been used for many years to maintain uniformity and continuity of assessment appraisals in Michigan. The use of these tables is required by the State Tax Commission.

Depreciation as used in this manual is expressed as a percentage good. It is a multiplier rather than a subtraction. To determine the age of a structure subtract the calendar year the building was built from the tax year for which the building is being appraised.

Very old buildings are depreciated until they reach the limit of the tables. In special cases, the limits of depreciation may be lower than the maximum in the tables. A percent condition, lower than that found in the depreciation table, should not be used unless something has caused the building to deteriorate faster than is indicated in the tables.

Economic Condition Factors

An ECF adjusts the assessor's use of the cost manual to the local market. County multipliers are provided by the State Tax Commission and adjusted annually to reflect change in the market of the construction costs found in the State Tax Commission Assessor's Manual and to "bring" those costs to the County level. Economic condition factors are adjusted annually by the assessor to further refine these costs to the local market.

An ECF must be determined and used in all cost appraisal situations where the *Assessor's Manual* is used. Saying "I didn't need to use an ECF because I used the new *Assessor's Manual*." Is not correct; even if the cost manual being utilized is brand new; it is a statewide manual and must be adjusted to local market conditions through the use of an ECF. It is also incorrect to indicate "I didn't need to use an ECF because I was valuing new construction" Again, an ECF must be used to adjust the statewide costs of the *Assessor's Manual* to local markets. An ECF must be used regardless of the age of the improvements being valued.

The single base for determining fair assessments is true cash value. What is the property worth? What would be the price an informed buyer would be willing to pay for the property in its condition and location? These are questions relating to true cash value. Assessments are to be set at 50% of the true cash value appraisals of each property. When appraising a mass of properties, the assessor frequently uses a cost-less-depreciation analysis and relates it to what properties are selling for through the use of an Economic Condition Factor (ECF). The ECF is derived by analyzing properties which have sold and comparing the cost less depreciation of the buildings to that portion of the sale prices attributable to those buildings. (This procedure will be discussed in detail later.) If there is a consistent relationship between the cost-less-depreciation analysis and the sale values of the buildings, this relationship is expressed

as an ECF which is used to adjust the cost-less-depreciation estimates to what properties are selling for in the market.

An ECF is calculated by analyzing verified property sale prices. The portion of each sale price attributed to the building(s) on the parcel is compared to the value on the record card of the same building(s). The ECF represents the relationship between the appraised value of the building as calculated using the Assessors Manual and the sale value of that building. When the building value is added to the value of the land and the land improvements, an indication of true cash value can be obtained for assessed valuations.

The verified sales used for an ECF analysis should generally be drawn from the same 24-month time period used for the sales study utilized for Equalization. From the examples below it can be determined that sales from October 1, 2007 through September 31, 2009 are used for both the sales study and ECF analysis for 2010.

The following guidelines must be considered when applying ECFs to appraisals:

1. The assessor should use the same time period of sales for the ECF study as used by the Equalization department in its study.
2. The same County multiplier should be used by the assessor as was used by the Equalization department.
3. The ECF is not applied to land and land improvements.
4. The ECF is applied only to buildings.
5. The ECF is not applied to "flat-valued" buildings.

Sample ECF Calculation

Sale Date	Sale Price	Land Value	Bldg. Value	RCN Less Depreciation	ECF
9/93	98,000	5,300	92,700	92,391	1.003
8/93	94,000	5,300	88,700	81,782	1.084
6/93	80,000	5,300	74,700	81,782	0.913
7/93	88,900	5,300	83,600	81,782	1.022
5/93	82,000	5,300	76,700	81,782	0.937
8/93	88,000	5,300	82,700	81,782	1.011

$$\frac{\text{Sale Price} - \text{Land \& Improvements}}{\text{Building Value}} = \frac{\text{RCN Less Depreciation}}{\text{ECF}}$$

Use of the Assessors Manual

Michigan Compiled Law (MCL) 211.10e indicates:

All assessing officials, whose duty it is to assess real or personal property on which real or personal property taxes are levied by any taxing unit of the state, **shall use only the official assessor's manual or any manual approved by the state tax commission**, consistent with the official assessor's manual, with their latest supplements, as prepared or approved by the state tax commission as a guide in preparing assessments. Beginning with the tax assessing year 1978, all assessing officials shall maintain records relevant to the assessments, including appraisal record cards, personal property records, historical assessment data, tax maps, and land value maps consistent with standards set forth in the assessor's manual published by the state tax commission.

The law requires that the *Assessor's Manual* be used as a guide in the property tax process—both for valuing property and for maintaining appraisal record cards, land value maps, etc. To create the manual, information from actual construction costs is compiled and organized; the costs contained in the manual represent actual construction projects for the manual's various occupancies. In developing the costs, special consideration was given to Michigan's climate.

The *Assessor's Manual* is used throughout the state to produce estimates of cost new for different types of structures (i.e., occupancies). These estimates of cost new are adjusted by County multipliers to localize the cost estimates to particular counties. Economic condition factors are used to further adjust the cost estimates for various neighborhoods or types of construction in certain localities.

The *Assessor's Manual* consists of two volumes. Volume I of the *Assessor's Manual* contains cost data for residential structures—including manufactured housing, mobile home structures, log homes, townhouses, and duplexes. Volume I also contains cost data for most agricultural structures. Volume II of the manual contains cost data for virtually all types of commercial and industrial structures. It also contains some cost data for some agricultural structures. Volume II also contains a section on unit in place (UIP) with breakdowns and details for building components.

ESTABLISHING CLASS OF CONSTRUCTION

One of the first steps in the cost approach is determining a quality of construction. The Assessor's Manual divides the "Residential Classes" of construction into six major categories, ranging from a class A at the highest level to a class D at the lowest quality level. The six major classifications have been broken down in the Assessor's Manual to assist in the proper determination of classification.

Adjustments to the classification are adjustments to the cost schedules in increments from the class C quality. The assessor must weigh all factors of the neighborhood with added attributes that are slightly greater or lesser than the next classification. The assessor must make an accurate assessment of the neighborhoods quality and

conditions to determine if an attribute is considered a plus adjustment or if the subject property is overbuilt for the neighborhood.

Every assessor must have a printed copy of the current State Tax Commission manual available in their offices. The manual is available for printing on the STC website.

HOW TO DETERMINE CLASS OF CONSTRUCTION

	Class D Economy	Class CD Tract Type	Class C Standard
	Constructed with cost as the primary determining factor. Materials and workmanship may or may not meet Federal or local building codes. Basement, if present, of minimum head room.	Constructed with materials and workmanship meeting minimum Federal and local building codes. Mass produced from standard plans, or prefabricated. The primary determining characteristic is that the residence is usually found among others of same design or with minor exterior modifications.	Construction with average quality materials and workmanship from stock-type plans with little or no architectural change. Some interior and exterior aesthetic features available as stock items. Built-ins few and of average quality. Interior surfaces drywall.
Exterior Walls			
Height	8 feet	8 feet	8 feet
Sheating	½" insulation board	½" insulation board	½" insulation board
Insulation	None	3-1/2" batt	3-1/2" batt
Interior	3/8" drywall	3/8" drywall	½" drywall
Roof			
	210# asphalt shingles	235# asphalt shingles	235# asphalt shingles
	3/8" plywood	3/8" plywood	½" plywood
	2" x 4" truss, 24" o.c.	2" x 4" truss, 24" o.c.	2" x 6" rafters, 16" o.c.
Interior Partitions			
Partition height	8 feet	8 feet	8 feet
Partition surface	3/8" drywall	3/8" drywall	3/8" drywall
Trim	Softwood	Softwood	Softwood
Floor finish	Softwood and linoleum or carpet and pad and linoleum	Softwood and vinyl, carpet and pad and vinyl sheets	Carpet and pad with under-layment and vinyl sheet
Basement walls	10 course, 8" concrete block	10 course, 8" concrete block	11 course, 8" concrete block
Basement floors			
Concrete	3" floor	3-1/2" floor	4" floor
Base	3" gravel base	4" gravel base	4" gravel base
Floor construction			
Subfloor	½" plywood	½" plywood	½" plywood
Joists	2" x 8", 16" o.c.	2" x 8", 16" o.c.	2" x 10", 16" o.c.

	Class BC Standard Deluxe	Class B Custom	Class A Class
	Constructed with average-quality materials and workmanship using modified stock-type plans. Built-ins of average to better than average quality. Some distinguishing interior and exterior qualities for individuality. Interior surfaces plaster.	Constructed with good-quality materials and workmanship from custom-made plans and specifications. Some built-ins and special interior and exterior features. Interior surfaces plaster. Roof with asphalt shingles.	Constructed with excellent-quality materials and workmanship. Includes many built-ins and special interior and exterior features. Interior wall surfaces are plaster. Roof with better than average shingles.
Exterior Walls			
Height	8 feet	8 feet	8 feet
Sheating	25/32" insulation board	5/32" insulation board	25/32" insulation board
Insulation	3-1/2" batt	3-1/2" batt	6" batt
Interior	Plaster on 1/2" drywall	Plaster on 5/8" drywall	Plaster on lath
Roof	290# asphalt shingles 5/8" plywood 2" x 6" rafters, 16" o.c.	290# asphalt shingles 5/8" plywood 2" x 8" rafters, 16" o.c.	290# asphalt shingles 1 x 6" plywood 2" x 8" rafters, 16" o.c.
Interior Partitions			
Partition height	8 feet	8 feet	8 feet
Partition surface	Plaster on 1/2" drywall	Plaster on 5/8" drywall	Plaster
Trim	Hardwood	Hardwood	Hardwood
Floor finish	Carpet and pad, hardwood, vinyl tile, ceramic tile	Carpet and pad, hardwood, vinyl tile, ceramic tile	Carpet and pad, hardwood, vinyl tile, ceramic tile, slate
Basement walls	11 course, 12" reinforced concrete block	12" reinforced concrete block	12" reinforced concrete block
Basement floors			
Concrete	5" floor	6" floor	6" floor
Base	6" gravel base	6" gravel base	6" gravel base
Floor construction			
Subfloor	5/8" plywood	5/8" plywood	5/8" plywood
Joists	2" x 10", 16" o.c.	2" x 12", 16" o.c.	2" x 12", 16" o.c.

MINIMUM RECORD CARD REQUIREMENTS

There are two different sections to an appraisal record card, the first is descriptive and the second is used to price out the various components. An appraisal record card is an inventory sheet first and a calculations sheet second. The following are items on the front of the State Tax Commission residential property record card (form 639, formally L-4188) are minimum requirements of a residential property record card.

Labeled spaces for the following:

- 1) Owner's name and room for address
- 2) Unit of government
- 3) Real property description
- 4) Parcel code number
- 5) Property address
- 6) Public improvements
- 7) Land value computations
- 8) Land improvements computations
- 9) Building value
- 10) Total value of property
- 11) Assessment history
- 12) Examination date

Space set aside for describing major structural components of residential buildings (e.g. windows, roof, interior, floors, ceilings, and electrical) including specific labeled spaces for the following:

- 1) Year built and year remodeled
- 2) Exterior wall type
- 3) Basement, crawl space, and/or slab on ground (may be noted on drawing)
- 4) Type of basement walls
- 5) Basement finish: specific space to note type of basement finish including "walkout"
- 6) Heat: specific space to note type of heat
- 7) Plumbing: specific space to make all entries requiring plumbing adjustments in the Assessor's Manual
- 8) Water & waste disposal: specific space to note whether there is public water, a well, public sewer, or a septic system
- 9) Built-ins: specific space to make entries requiring adjustment: under the heading "Built Ins" in the Assessor's Manual
- 10) Fireplaces: specific space for making entries requiring adjustments under "Fireplaces" in the Assessor's Manual
- 11) Porches: specific space to note type and size of porches and decks
- 12) Garage: specific space to make all notes needed to accurately price garages and carports
- 13) Class of house

- 14) Size for rates
- 15) Space for a sketch of the house
- 16) An area for calculating cost new less depreciation including a specific space for County multiplier, depreciation, and ECF multiplier

There should also be sufficient space to handle the pricing of breezeways, solar rooms, Michigan basements, and living area overhang.

The format of the descriptive portion of the record card must use the same numbering system as found on the record card in the Instructions chapter of Volume I of the Assessor's Manual. The format of the pricing section of the record card must be easily understood and easily traceable back to the descriptive section of the card.

Pricing Section of a Record Card

The following help make the pricing section of a record card easily understood and easily traceable back to the descriptive section of the card.

- 1) The pricing section should use the same numbering system as the descriptive section of the card.
- 2) A reader should be able to identify which individual items are priced as adjustments and additions and what their prices are.
- 3) Adjustments and additions for items in the same category or sub-category in the Assessor's Manual should be priced together in the same place. Thus a garage and garage finish should not be priced in two different areas.
- 4) The County multiplier, the % good depreciation multiplier, and the ECF multiplier should each be listed separately and not be combined with each other. Of these three, the ECF should appear last. The best arrangement is to multiply base costs by the County multiplier to get an estimate of cost new, then multiply cost new by the depreciation multiplier to get depreciated cost, and finally multiply depreciated cost by the ECF to get an estimate of true cash value for the building improvements.
- 5) The use of abbreviations is discouraged. The porch abbreviations in the manual may be used.

General Information Regarding Measuring a Building

Specific property data must be comprehensive enough to:

- Provide the data needed to process each parcel of property to an indication of value
- Generate the tax roll and related tax accounting output
- Provide assessing officials with a permanent record to facilitate maintenance functions and to administer taxpayer assistance and grievance proceedings.

The data gathered should include the parcel identification number, ownership and mailing address, legal description, property address, property classification code, local

zoning code, neighborhood identification code, site characteristics, and structural characteristics.

All the data should be recorded on a single property record card, the format of which has been approved by the State Tax Commission. The specific property data will be compiled from existing assessing records and field inspections. The parcel identification number, ownership, mailing address, and legal description will be obtained from existing tax rolls. Property classification codes will also be obtained from existing tax rolls (whenever available) and verified in the field. Local zoning codes will be obtained from existing zoning maps. Neighborhood identification codes will be obtained for the neighborhood delineation maps. Sizes and acreage will be obtained from existing tax maps. The property address and the site and structural characteristics will be obtained by making an exterior and interior inspection of each property.

Field inspections must be conducted by qualified individuals and if not the assessor, under the close supervision of the assessor. Each property must be personally visited and the following information should be collected:

- Verify the ownership. If rental property, collect information. If a transfer has occurred collect sales information.
- Record the property address.
- Verify the current property classification
- Verify zoning codes and permitted uses.
- Inspect the interior of the building (if allowed access) and record all pertinent physical.
- Measure and inspect the exterior of the building, as well as all other improvements on the property, and record the story height, and dimensions and/or size of each.
- Record a sketch of the principle building(s), consisting of a plan view showing the main portion of the structure along with any significant attached exterior features, such as porches, etc. All components must be identified and the exterior dimensions to the nearest six inches shown for each.
- Select and record the proper quality grade of the improvements.
- Select and record the proper costs or cost adjustments for all field priced items.
- Review the property record card for completeness and accuracy.

Complete and accurate data are essential to the program. Definite standardized data collection and recording procedures must be developed and followed. When preparing a replacement cost estimate of a residential structure, assessors should follow an established routine to avoid omitting details which might necessitate a trip back to the property. The normal procedure is:

- Start with the exterior inspection, measurements and description.
- Move to interior inspection and description if allowed inside the home.
- Measure and describe the outbuildings and miscellaneous items.
- Price the nonstandard items.

- Determine the class of construction.
- Determine the depreciation or percent good.
- Don't forget to photograph the major structures on the property. With this, the field work on the appraisal card is now complete and the card is ready to complete the replacement cost estimate.

All dimensions should be to the nearest half-foot. Drop measurements under four inches; add measurements over four inches to the nearest half-foot.

An assessor's equipment should include a 50-foot cloth tape, clipboard, a small plastic scale, a supply of well-sharpened pencils and a camera.

A good process starts in the office by printing off copies of the current appraisal record cards, sketches and photos. Obtain a line map with parcels and roads and an aerial with the line map overlaid.

When arriving at the property, it is always a good idea to check for dogs first before getting out of the vehicle. If the owner is home, discuss why you are there and what you are there to look at. If the owner asks you to leave the property, you have to leave. If no one is home, leave a card or letter in the door explaining why you were there. You can't go inside buildings unless invited by the homeowner and certainly can't peek in windows to see what the inside of the home looks like.

Photographing the Property:

Photograph the major structures and other structures. Attach the photograph to the "residential property record card" in the appropriate place. Whatever photographing method you use, be sure the photographs are clear. Start by taking photos of the house and any outbuildings. You should take photos of all sides of the house so you can later see where the first story stopped and the second story started.

Measurement and Exterior Inspection:

Start the measurements at either the left front or right front corner of the structure. At the same time, mark the starting point on the grid in either the lower left-hand or lower right-hand portion of the grid. Measurements can start either clockwise or counterclockwise around the house, using outside measurements.

Try to pick up decks and sidewalks etc as you move around the structure. Also try to measure the distances of various components from a certain point (the 6 x 12 deck is 6 ft from the corner or the 1 story addition is 8' past the 2 story part, although not actual square footage dimensions, they do provide locations). Many times those odd dimensions will help close a sketch or help to figure out what the square footage is of a certain part.

The road is always at the bottom of the sketch with the sketch oriented to the road; if not set up this way, then a note explaining why must be included. Most assessors sketch a box with the dimensions in the approximate location and for various outbuildings and later do a proper sketch, Windows in the foundation are a good indication of a basement, vents of a crawl space, a door less than a foot off of the ground is a good indication of a slab.

Interior Inspection and Description:

If the taxpayer grants you access to the inside of the house you can make a careful inspection of the interior finish and construction details and record these details in the appropriate place on the cost record. Note all details which vary from the base for the construction class so that proper adjustments can be made.

Other Improvements—Measurement and Inspection:

Measure and inspect other improvements on the property such as concrete flat work, detached garages, patios, sheds, etc that you did not pick up when doing your initial measurements. Where possible, show these on the diagram at their approximate location, and enter and describe them in the proper place on the cost record. If there is more than one major structure on the property, use a separate card for each. Then number the cards 1 of 2, 2 of 2, etc.

Pricing Nonstandard Items:

Nonstandard items may include fireplaces, patios, barbecues, sheds, fences, sprinklers, pools (in ground and above ground), ponds, gazebos, etc. By referring to the various sections of the manual, you will build up unit costs for these items, then enter them on the record card at the appropriate place.

Class of Construction and Depreciation:

You have now thoroughly inspected the property, determined its age, observed its condition, and are prepared to determine the class of construction and estimate the depreciation, or more properly, the remaining percent good.

If the condition of the structure is average for its age and shows no signs of excess depreciation or does not reflect conditions which would warrant increasing the percent good, the percent good reflected by the actual age is sufficient. If, however, either of the above conditions exist, adjust the depreciation upward or downward in the depreciation section of the cost record.

Keep in mind several issues as you are updating record cards and remember every community is different:

1. Some owners do excellent maintenance, some just “get by” and others don’t do any.
2. Does the level of maintenance affect the structural integrity?
3. When property sells, most people fix it up – few sell as is.

By now, you are sufficiently familiar with the structure to determine the class of construction. Compare structural and finished details with the base specifications in the manual to find the proper class of construction. Then enter the details in the appropriate place on the record card.

Chapter 12

Sales Comparison Approach

The sales comparison approach to value estimates the value of property by applying verified data from the market. Sales data is related to the property being appraised by comparison. The sales comparison approach is also known as the comparison method.

The sale price paid for a property does not necessarily dictate the market value of the property. If one buyer was uninformed regarding the real estate market and another buyer was very familiar with the real estate market, you would have two different values for a property. Another reason the sale price does not always reflect market value is that one of the parties could be under duress. A job transfer may necessitate the sale of a home and it may be sold for less than market value because of the need to relocate immediately. A divorce is another reason a quick sale may be necessary. You must review each sale to determine if it is a valid sale.

The definition of market value employed by the Appraisal Terminology and Handbook is: "The most probable price in terms of money which a property will bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller, each acting prudently, knowledgeably and assuming the price is not affected by undue stimulus."

This definition implies that: the sale will be completed by a certain date; buyer and seller are typically motivated; both parties are well informed; there has been sufficient exposure on the open market; payment is made in cash or its equivalent; financing is on terms generally available in the community at that date and are typical for the property; and the price represents a normal consideration for the property sold unaffected by special financing amounts or terms, services, fees, costs, or credits incurred in the transaction.

Market Value

Market value:

1. Is the highest price, or represents the usual selling price?
2. Is expressed in terms of money?
3. Results from proper exposure on the market?
4. Is the result of the actions of an informed buyer?
5. Is the result of a conclusion of an informed seller?
6. Recognizes the present and potential use of the property?
7. Is arrived at in an atmosphere of freedom from compulsion?

Every sale used in the comparison process must meet these standards to be considered a valid sale.

The principle of substitution is applicable in the sales comparison approach. The substitution in this case is that a buyer will not pay more for a property than it will cost to buy an equally desirable property.

The substitute property must be able to be bought in a reasonable amount of time and offer similar use and function.

There are four basic steps in the sales comparison approach:

1. You must select sales of comparable properties.
2. List the sales.
3. Adjust the sales TO THE SUBJECT and tabulate.
4. Correlate and justify the value of the subject property.

Sources of sales data:

1. Register of Deeds office.
2. Real estate brokers.
3. Appraisers.
4. Newspaper articles.
5. Classified ads.
6. Property Transfer Affidavits.
7. Office files.
8. Talking to the sellers and buyers of the property.

You should verify all sales with one of the parties — the buyer, seller, or broker. Verify the information regarding price, down payment, mortgage amount, buyer financing, relationship between buyer/seller, exposure on the market, and if any personal property was included.

You should develop a sales data file. Keep all information you receive on a property sale in one place. The register of deeds is also a good source of sales. You can also contact the buyer or seller or the broker who handled the sale.

All sales should be verified with two sources. If you have a deed or a transfer affidavit, the second source could be the buyer/seller or broker. If there is a difference on the selling price, you should go to a third source and use the two prices that are alike as your selling price.

If a sale is out of line with the other comparable sales, find out if there were unusual circumstances such as: it is a family sale; the transfer is between a corporation and its stockholders; it is only part of a property; it is a bankruptcy sale; it is a sale of an undivided interest; it is a sheriff's deed; or it is a foreclosure or similar sale.

Sales data is available in the assessor's office due to the requirement of Proposal A that all property transfers be filed with the local assessor. The Property Transfer Affidavit can also be used to verify sales.

Gathering Sales Data

Sales or market data is information about property prices. It may include offers to buy or sell property as well as actual sales prices.

You must use comparable properties. Comparing a 3-bedroom ranch with a 3-bedroom colonial is not comparing like properties. Comps must be similar to the subject. It should be a current sale, it should be verified, and it should also be a qualified sale. Some items you might look at in qualifying a sale are location, zoning, improvements and services, traffic patterns, and similar size and shape of lots.

After you have gathered your sales data, you need to verify the information. The buyer, seller, or real estate agent involved in the sale is your best source. If you are unable to confirm information with any of these people, you can use the Property Transfer Affidavits and the Register of Deeds.

Next, you qualify the sale. In addition to the arm's length, informed buyers, no undue duress, and adequate exposure requirements, there could be special circumstances in the sale that must be considered. Common examples of special circumstances would be land contract payoffs, sheriff's deeds, estate sales, tax sale deeds, and bankruptcy deeds.

There are thirty types of deeds or instruments of transferring property. You must read the entire deed to determine if it is a valid sale.

Unit Selling Price

After you have gathered the sales data, compare the information with other properties that have sold. Different types of property have specific units of comparison to use. Some examples (not an all inclusive list):

1. Vacant land is done by either square foot, front foot, per acre, per lot, and per buildable unit.
2. Farm land is done by price per acre.
3. Commercial land is done by front foot price or square foot.
4. Industrial land is done by square foot price.
5. Residential land is done by equivalent front foot or price per lot.
6. Residential improved is done by sale price per square foot of first floor area.
7. Commercial is done by square foot price of gross leasable area or net rentable area.

8. For commercial properties, there are specific sub-categories that may be used.
9. Industrial is done by sale price per square foot.

It is important that you compare the type of conveyance, terms of sale, condition of the property, location, and characteristics of the improvements.

When you are doing an appraisal, it is important to be consistent. It is a good idea to develop a form to use and use it every time. If you use a form, you will be assured that you have considered everything that is necessary to determine the correct value. Some items you should include on your form are location, surroundings, traffic, lot size, improvements and services, driveway, building interior specifics, and amenities of the property.

You should develop a format for recording data. The format +, -, and = may work for simple appraisals.

Gross Rent Multiplier

Gross rent multipliers are used to value income-producing residential property.

Gross rent multipliers are numbers expressing the ratio between the sales price of residential property and its monthly unfurnished rent. When residential properties are rented in sufficient number in a market, the sales price and the gross monthly unfurnished rent of similar properties will tend to move in the same direction because they are subject to the same market forces. The ratio between sales price and gross rents tends to be fairly consistent for similar properties under the same market conditions.

The application of gross rent multipliers requires three steps:

1. Estimate the current monthly market rent of the subject property.
2. Calculate the appropriate gross rent multiplier (GRM) from sales of comparable properties that were rented at the time of sale. Sales price divided by gross rent equals the gross rent multiplier.
 - $\text{SALES PRICE} \div \text{GROSS RENT} = \text{GROSS RENT MULTIPLIER}$
3. Multiply the market rent of the subject property by the gross rent multiplier to obtain an estimate of market value of the subject property.
 - $\text{MARKET RENT} \times \text{GROSS RENT MULTIPLIER} = \text{MARKET VALUE}$

Chapter 13

Income Approach

The income approach considers the income a property can earn for its owner. It is most often used when the market is more responsive to the income stream of a property or when comparable sales data is not available. Investors will not purchase income-producing property unless they can obtain a reasonable return on their investment. If an investor can earn 6% by purchasing bonds and 4% purchasing a building, a prudent investor would be more inclined to buy bonds.

The value of an income-producing property is set by the income it has historically earned and the potential it has for a future income stream. If the assessor can estimate a stabilized income stream, property value can be determined using the income approach.

The income approach uses both the principles of substitution and anticipation. The principle of anticipation states that the market value is the present worth of all the anticipated future benefits to be derived from the property. With the income approach, potential gross income is estimated by reviewing market data that includes the historical income. After allowing for estimates of vacancy and collection loss, miscellaneous income, and appropriate operating expenses, the net operating income is derived. A capitalization method is then chosen to obtain the capitalization rate that is used to calculate the estimated market value.

The income approach can be broken down into two components: Determination of net operating income and development of a capitalization rate. Each of these components has multiple steps in their development. Let's start with the development of net operating income.

Component 1: Development of Net Operating Income:

The development of net operating income involves four steps: Estimating potential gross income, estimating vacancy and collection loss, estimating effective gross income and determining operating expenses.

Step 1: Estimating Potential Gross Income

Potential gross income is market rent times the number of units available to rent. Potential gross income estimates the amount of rent a property could command on the open market if rented at 100 percent occupancy.

There are two types of rent.

- a) Market rent is the rent that a property could command on the open market.
- b) Contract rent is the rent actually received for a property as designated by the lease.

Potential gross income is estimated using market rent. To estimate market rent for a property, you analyze the income of comparable properties and the past, present, and future projected income for the subject property.

Market rent is used rather than contract or actual rent because the subject property may be rented for more or less than the rent that could be commanded on the open market. The use of contract or actual rent in that case would distort the market value of the subject property.

Market rental information can be gathered from:

- a) Leases which are contracts in which the property rights are transferred in exchange for rent.
- b) Survey of commercial property owners and tenants. The survey can be made by mailing an income information request to commercial property owners or by contacting tenants. The survey must include rental and expense information; which expenses are paid by the owner and which expenses are paid by the tenant.

When rental information is collected it is important to consider the rental units of comparison. Three of the most common rental units of comparison are:

- a) Rent per number of bedrooms in an apartment (1-bedroom, 2-bedroom).
- b) Rent per room.
- c) Rent per square foot of floor space.

Step 2: Estimating Vacancy and Collection Loss Rates

The vacancy and collection rate an income producing building realizes is based upon factors that affect the quantity and quality of the income generated by the building. Those factors include condition and location of the building, age, style and design of the building and the type of tenants leasing space in the building.

The following vacancy information is gathered from buildings that are similar in every way to the subject property, including location.

Apartment Building	Number of Apartments	Apartments Vacant
A	70	3
B	100	5
C	124	7

The vacancy rate is estimated as follows:

Apartment Building	Number of Apartments	Apartments Vacant	Vacancy Rate
A	70	3	$3 \div 70 = .043$
B	100	5	$5 \div 100 = .050$
C	124	7	$7 \div 124 = .057$

The collection loss is estimated as follows:

Apartment Building	Number of Units	Rent not Collected	Potential Gross Income	Collection Loss Rate
A	70	\$ 7,560	\$ 756,000	.010
B	100	\$17,100	\$1,140,000	.015
C	124	\$26,040	\$1,302,000	.020

The income loss for a building rented at market rent with 70 rental units is estimated to have a 1 percent collection loss rate ($\$7,560 \div \$756,000 = .01$ or 1 percent). A building with 124 apartments is estimated to have an income loss rate of 2 percent ($\$26,040 \div \$1,302,000 = .02$ or 2 percent). The income loss rate increases as the amount of collectable rent increases and likewise, the higher the rent the higher the rent loss.

The vacancy and collection loss rate is calculated by adding together the vacancy rate and the collection loss rate.

Step 3: Calculating Effective Gross Income

Effective gross income is defined as the potential gross income less the vacancy and collection loss plus other income or miscellaneous income.

Problem A

We are appraising an apartment building that has 25 one-bedroom apartments. A study of the market indicates that one-bedroom apartments of this type, age, and location rent for \$800 per month. Further study tells us that the market indicates a 5 percent vacancy and collection loss rate for this type and location of one-bedroom apartments. The miscellaneous income this building generates consists of \$700 per month for laundry facilities and \$700 per month for carports.

Answer the following questions using the given information.

- What is this building's estimated potential gross income?
- What is this building's estimated vacancy and income loss?
- What is the miscellaneous income generated by this building?
- What is the estimated effective gross income for this building?

Answer:

- $\$800$ per month rent x 25 apartments x 12 months = \$240,000
- $\$240,000 \times 5\% = \$12,000$
- $\$700$ for laundry facilities + $\$700$ for carports x 12 months = \$16,800
- $\$240,000$ (potential gross income) – $\$12,000$ (vacancy and collection loss) + $\$16,800$ (misc. income) = \$244,800

Step 4: Estimating Allowable Expenses

Allowable expenses are estimated through the use of market information. Certain expenses are not allowable because those expenses are not necessary for generating income or because those expenses are a component of the capitalization rate, these include: Depreciation, mortgage interest or mortgage payments including the interest on the mortgage and property taxes.

Other expenses that are not allowed include: Capital improvements because they generally increase the income generated by the property, owner's costs and corporation costs because they are an expense against the type of ownership, and income taxes because they are an owner's expense.

Allowable Expenses	Non-Allowable Expenses
Advertising	Capital Improvements
Bookkeeping	Depreciation
Cleaning Supplies	Income Taxes
Lawn Care	Mortgage Payments
Legal Fees	Property Taxes
Maintenance	
Office Supplies	
Repairs	
*Reserves for Replacement	
Salaries	
Snow Removal	
Utilities	

*Reserves for replacement are a category of allowable expenses that allows the owner to set aside a fund for replacement of short-lived items and to claim that reserve fund as an allowable expense. The annual amount allowable is the cost divided by the estimated life of the item.

Item	Cost	Life	Reserves for Replacement
Stove	\$ 600	10 Years	\$ 60
Refrigerator	\$ 800	10 Years	\$ 80
Furnace	\$ 1,500	15 Years	\$ 100
Roof Cover	\$10,000	30 Years	\$ 333
Interior Painting	\$ 5,000	3 Years	\$1,666
Carpeting	\$10,000	10 Years	\$1,000

Component 2: Determining a Capitalization Rate

Capitalization rate is defined as a rate that represents a relationship between income and value. The capitalization rate involves the calculation of three items and is the sum of the discount rate, the recapture rate, and the effective tax rate.

1. Discount rate is the rate of return on the investment.
2. Recapture rate is a rate for recovery of the investor's investment in the building. The investment in the land is recovered through the sale of the land after the end of the economic life of the building.
3. Effective tax rate is the rate of return necessary to cover payment of the property taxes.

Step 1: Development of the Discount Rate:

The discount rate is the rate of return on the investment and can be developed in three ways:

- A. Summation Method
- B. Band of Investment Method
- C. Market Comparison Method

Summation Method: The summation method considers that there are 4 components that an investor considers when determining the discount rate:

1. Safe Rate: earned on savings deposited in a bank or other safe investment.
2. Non-Liquidity: time involved in converting the investment into cash.
3. Risk: risk involved in the investment.
4. Management: management of the invested funds.

Example:

Rate Earned on a Passbook Savings Account	2.5%
Rate for Non-Liquidity	0.5%
Rate for Risk Involved in the Investment	4.0%
Rate for Management of Investment Funds	0.5%

Solution

Safe Rate	.025
Non-Liquidity Rate	.005
Risk Rate	.040
Management Rate	<u>.005</u>
Discount Rate by Summation Method	.075 or 7.5%

Band of Investment Method: The band of investment method is a weighted average of the owner's investment rate and the mortgage rate for the investment property.

Example: An investor acquired a mortgage covering 80% of the investment. The balance of the investment was 20% owner's equity. The interest rate on the mortgage was 7.5%. The investor expects a 10% rate of return on the equity investment.

Solution

	Investment Ratio		Rate		
Mortgage	.80	x	.075	=	.060
Investor's Equity	.20	x	.100	=	<u>.020</u>
Discount Rate using the Band of Investment Method = .080 or 8%					

Market Comparison Method: When developing the discount rate by the market comparison method, net income after extraction of recapture and taxes is divided by the sale price.

Sale No.	Net Income After Extraction of Recapture and Taxes	÷	Selling Price	=	Discount Rate
1	\$20,000	÷	\$200,000	=	.10
2	\$ 6,250	÷	\$ 62,500	=	.10
3	\$12,500	÷	\$125,000	=	.10

The discount rate by the market comparison method = .10 or 10%.

Step 2: Development of the Recapture Rate

Recapture rate is the return of the investment and can be developed in two ways: Remaining economic life method and market comparison method.

Remaining Economic Life Method: The remaining economic life method of developing the recapture rate uses the remaining economic life because the investment must be recaptured during the remaining economic life of the property. 100% is divided by the remaining economic life of the property.

$$100\% \div 25 = .040$$

$$100\% \div 50 = .020$$

$$100\% \div 30 = .033$$

$$100\% \div 70 = .014$$

Market Comparison Method: The market comparison method of developing the recapture rate uses net income after extraction of discount dollars and taxes divided by the selling price of the building.

Sale No.	Net Income After Extraction of Discount and Taxes	Selling Price	Land Value	Building Selling Price	Recapture Rate
1	\$3,000	\$150,000	\$50,000	\$100,000	.030
2	\$4,250	\$180,000	\$35,000	\$145,000	.029
3	\$2,750	\$125,000	\$28,750	\$ 96,250	.029

The recapture rate by the market comparison method = .03 or 3%.

Step 3: Development of the Effective Tax Rate:

The effective tax rate is the ratio of property taxes to the market value of the property. The effective tax rate can be developed by only one method; Tax Rate Times Assessment Ratio Method.

Township	Tax Rate	x	Assessment Ratio	=	Effective Tax Rate
A	48 Mills or .048	x	50% or .50	=	.024
B	58 Mills or .058	x	50% or .50	=	.029
C	65 Mills or .065	x	50% or .50	=	.033

Calculate the effective tax rate for a Township with a tax rate of 55 mills.

55 Mills or .055 x 50% or .50 = .0275

Effective Tax Rate = .0275 or 2.75%

Final Development of the Capitalization Rate:

The capitalization rate is the sum of the discount rate, the recapture rate, and the effective tax rate.

Discount Rate (average of the 3 methods)	8.0%
Recapture Rate (average of the 2 methods)	2.5%
Effective Tax Rate	<u>2.8%</u>
Capitalization Rate	13.3%

Calculate the capitalization rate given the following information: The mortgage is 80% of the selling price and interest rate is 7.5%. The investor requires a 10% return on the equity investment. The property has a remaining economic life of 50 years. The tax rate in the City in which the property is located is 60 mills. The assessment ratio is 50 percent of true cash value.

$$\begin{aligned}
 \text{Discount Rate: (Mortgage)} & \quad .80 \times .075 = .06 \\
 & \quad \text{(Equity)} & \quad .20 \times .10 = \underline{.02} \\
 & & \quad \underline{\underline{.08}}
 \end{aligned}$$

Recapture Rate: $100\% \div 50 \text{ Years} = .02$

Effective Tax Rate: $60 \text{ Mills} \times .50 = .03$

Capitalization Rate: $.08 + .02 + .03 = .13 \text{ or } 13\%$

The **Overall Rate** is a weighted capitalization rate that represents a direct ratio between net income and sale price or value.

Land Rate contains:

- A. Discount Rate
- B. Effective Tax Rate

Building Rate contains:

- A. Discount Rate
- B. Effective Tax Rate
- C. Recapture Rate

Overall Rate contains:

- A. Discount Rate
- B. Effective Tax Rate
- C. Recapture Rate for the building

The overall rate contains a recapture rate that is weighted so that only the value of the building is recaptured over the remaining economic life. The land will not depreciate and that portion of the investment will be recaptured after the economic life of the building has expired through the sale of the land.

For example, this property has a land value of \$50,000, a building value of \$200,000, and net income of \$30,000.

Land Capitalization Rate		Building Capitalization Rate		Overall Rate	
Discount Rate	.080	Discount Rate	.080	Discount Rate	.080
Effective Tax Rate	<u>.024</u>	Effective Tax Rate	.024	Effective Tax Rate	.024
		Recapture Rate	<u>.020</u>	Recapture Rate	<u>.016</u>
	.104		.124		.120

Land Value	\$ 50,000	x .104	= 5,200	Income Attributable to Land
Building Value	200,000	x .124	= 24,800	Income Attributable to Bldg
Property Value	\$250,000	x .120	= \$30,000	Net Income

The recapture rate component of the overall rate can be calculated as follows:

$100\% \div 50 \text{ years remaining life of the building} = .02$ recapture rate for the building
 Building-to-land ratio: 80/20

Recapture rate: $.02 \times 80\% \text{ building} = .016$

Overall rate = $.016$ (recapture) + $.08$ (discount) + $.024$ (effective tax)

Calculate the overall rate given the following information.

Land-to-Building Ratio 30/70
Remaining Economic Life 25 Years
Discount Rate .070
Effective Tax Rate .028

Recapture Rate	$100\% \div 25 = .04; .04 \times .70 = .028$
Discount Rate	.070
Effective Tax Rate	<u>.028</u>
Overall Rate	.126

The weighted overall rate is developed from the market. It is a ratio of net income to selling price or value.

Net Income	÷	Selling Price	=	Overall Rate
\$12,000	÷	\$100,000	=	.12

Calculate an estimated overall rate from the following market information.

Sale No.	Net Income	Selling Price	Overall Rate
1	\$30,000	\$250,000	.120
2	\$57,500	\$487,500	.118
3	\$46,250	\$380,000	.122
4	\$24,500	\$204,000	.120
5	\$41,250	\$341,000	.121

The indicated overall rate (by taking the average) = $.12$ or 12%.

Capitalization Techniques

Capitalization is the process of converting anticipated future income into present value.

Capitalization techniques:

- A. Land Residual
- B. Building Residual
- C. Direct Capitalization

The Land Residual Technique refers to the residual net income that is left after recapture, discount, and taxes for the building have been deducted. The remaining or residual net income will be capitalized into the land value.

The Building Residual Technique refers to the residual net income after discount and taxes for the land have been deducted. The remaining or residual net income will be capitalized into the building value.

The Direct Capitalization Technique uses the overall rate to capitalize net income into an estimation of property value. The appraiser will determine which technique to use by analyzing the property and the market information available to value that property.

1. Land residual technique is used when:
 - a. Land value can not be determined due to the lack of market or sales information.
 - b. The building is new and easy to value.

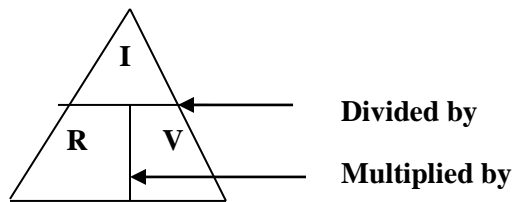
2. Building residual technique is used when:
 - a. The building is not new and can not be accurately valued.
 - b. The land can be easily valued due to adequate sales information.
 - c. The building is not the highest and best use of the land.

3. Direct capitalization technique is used when:
 - a. Sales information is available.
 - b. Neither the land value nor the building value is known.

Putting it All Together – The IRV Formula:

When valuing property by any one of the techniques, use the IRV formula. There are variations to the IRV formula which allow you to calculate the third component given two of the three components.

IRV – I = Income
 R = Rate
 V = Value



I (Income)	÷	R (Rate)	=	V (Value)
I (Income)	÷	V (Value)	=	R (Rate)
R (Rate)	x	V (Value)	=	I (Income)