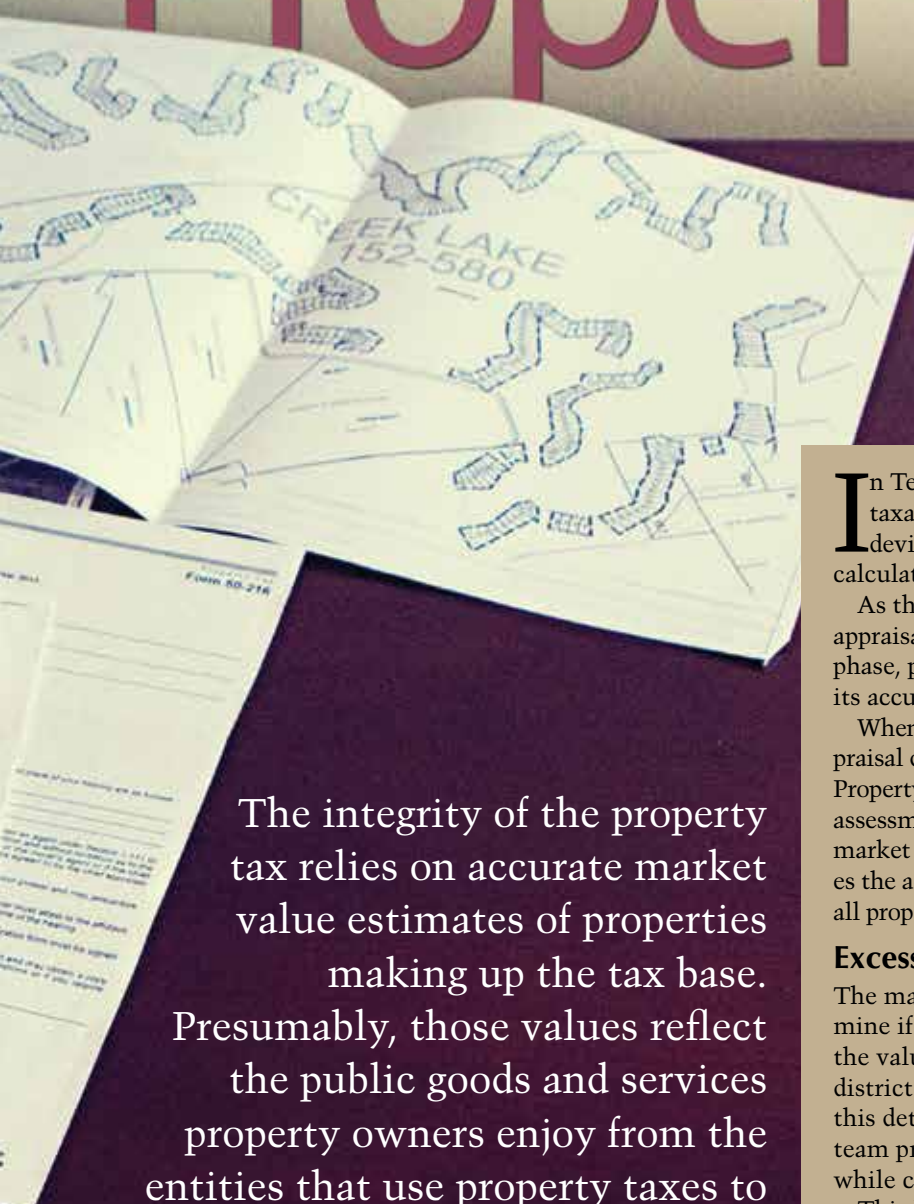


# Property Tax

## Protest & Appeal

By Charles E. Gilliland



The integrity of the property tax relies on accurate market value estimates of properties making up the tax base. Presumably, those values reflect the public goods and services property owners enjoy from the entities that use property taxes to fund their operations. However, the market value of any particular property is unknown unless the property changes hands in a free-market exchange. To implement an annual property tax, officials must estimate market values for all properties each year.

In Texas, county appraisal districts determine the value of each taxable property. The annual cycle begins with the district devising an appraised value designed to serve as the basis for calculating the owner's tax liability.

As the spring unfolds, the property tax cycle moves from the appraisal phase to the equalization phase. During the equalization phase, property owners can review the appraised value to evaluate its accuracy.

When owners disagree with the estimates presented by the appraisal district, they can take advantage of remedies provided by the Property Tax Code to adjust appraisals that do not represent a fair assessment of their properties. Those remedies focus on two issues: market value and equal and uniform appraisals. The former addresses the accuracy of the value estimate; the latter seeks to ensure that all property owners are treated fairly in the assessment process.

### Excessive Appraisal

The market value remedy may require a district court to determine if the appraised value on the appraisal district's roll exceeds the value required by law. The court must decide if the appraisal district missed the mark in estimating property value. Typically, this determination involves teams of dueling experts with each team producing and defending an appraisal of the subject property while criticizing the judgments and conclusions of other experts.

This kind of confrontation occurs owing to the subjective aspects of deciding "market value." Definitions of market value ultimately require an estimated value that complies with legal requirements. Official formulations contain specifications of characteristics a transaction must meet to be considered evidence of market value. Those requirements roughly distill to an amount reflecting the probable price a property would command in an open and competitive market transaction.

Appraisal at all levels calls for circumstances often at variance with actual conditions observed in contemporary economies. Client's intended use, principals' motivations, number of competitors and a myriad of other circumstances can impact observed market transactions. All of these factors drive modern appraisal applications. These complicating factors guarantee that no single hard-and-fast formula can reliably produce a credible estimate of market value.

Rather than an immutable mathematical algorithm, appraisal is an interpretive art. An appraiser is called upon to skillfully transform market information into an estimate of value for a subject property. That estimate must reflect the realities of the economic and legal environment of that subject property. The results rely on a set of assumptions and interpretations designed to capture those realities.

Clearly, differences in assumptions and interpretations can produce different bottom line estimates. The court must decide which competing analysis most closely approximates the value required by the Property Tax Code. The court might also decide that neither appraisal is correct and, therefore, settle on a different value. The amount specified by the court becomes the value used to determine the property tax liability.

## Unequal Appraisal

The Texas Constitution calls for equal and uniform treatment of property owners. That provision prohibits discriminatory practices in assessing taxes. For example, suppose an assessor appraises sold properties at or near their sales price while leaving other properties' taxable values unchanged. Over time, disparities created by this practice would result in significantly different tax liabilities for similar properties.

The equal and uniform provision allows property owners to protest or appeal when their properties have been appraised by a different standard than other properties. That means that even if the appraisal district value does not exceed market value, an owner can seek relief if the property was treated differently from other properties in the tax base.

The district court must grant relief when presented with evidence proving that a subject property was appraised unequally. The Property Tax Code specifies the following as evidence of such appraisals:

- the appraisal ratio of the property exceeds by at least 10 percent the median level of appraisal of a reasonable and representative sample of other properties in the appraisal district;
- the appraisal ratio of the property exceeds by at least 10 percent the median level of appraisal of a sample of properties in the appraisal district consisting of a reasonable number of other properties similarly situated to, or of the same general kind or character as, the property subject to the appeal; or
- the appraised value of the property exceeds the median appraised value of a reasonable number of comparable properties appropriately adjusted.

The first two provisions require substantial resources to establish the appraisal ratios of a sample large enough to meet standards of statistical testing. Because of the expense implied by those tests, many unequal appraisal protests and appeals rely on the third option.

Some controversy has arisen concerning this specification of the code, which does not define "reasonable number" and "appropriately adjusted." Instead, the code leaves that determination to analysts preparing studies of sampled properties. Such studies typically examine the appraisals of a set of similar

properties after adjustments are made for differences from the subject. The studies are designed to identify valuation differences between the subject and the sample.

In addition to quarrels over the sample contents and adjustments made, this provision calls for a departure from the market value standard of taxation. Specifically, critics argue that granting relief by reducing the subject's appraised value to the median value of the sample results in an unconstitutional departure from taxation based on market value, which the Texas Constitution requires. In essence, they reason that this provision allows taxpayers to use an artificially low value as the basis for their property tax liability.

In Harris County Appraisal District (HCAD) v. United Investors Realty Trust, the Court of Appeals of Texas, Houston (14<sup>th</sup> District) addressed these issues. An expert witness for the taxpayer, owner of a neighborhood shopping center, found the median appraisal of a sample of seven comparable properties to be \$62.71 per square foot while the subject property appraisal amounted to \$85.13 per square foot.

The HCAD appraisal of the subject property followed from a recent purchase by United Investors Realty Trust. The sale price exceeded the HCAD appraisal by more than 9 percent. Despite these facts, the court found the taxpayer expert's analysis to be compelling evidence of unequal appraisal and reduced the subject taxable value. Responding to HCAD's argument that the result did not reflect the "market value" of the subject as required by the Texas Constitution, the court noted, "If a conflict exists between taxation at market value

and equal and uniform taxation, equal and uniform taxation must prevail."

At first, it might appear that the court condoned an egregious violation of property tax policy by abandoning the market value standard. However, further reflection suggests that the properties making up the sample in the study had been valued at far less than a valuation based on the United Property sale would justify. The ruling seems to suggest that HCAD may have erred by not raising appraisals on all properties based on the new data point.

However, one sale does not provide conclusive proof that a market has risen. Additional sales at higher values might confirm the increased appraised value and justify a revaluation. Meanwhile, raising one property without raising others would unjustly penalize the owner of that property. The unequal appraisal provision appears to be aimed at avoiding this, even if the property is taxed at a level below market value. 📌

*Dr. Gilliland (c-gilliland@tamu.edu) is a research economist with the Real Estate Center at Texas A&M University.*

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## THE TAKEAWAY

High effective tax rates in Texas give rise to confrontations between taxpayers and appraisal districts as property owners seek to minimize their tax liabilities. Many of those disagreements will likely continue to focus on unequal appraisal.



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Texas A&M University  
2115 TAMU  
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<http://recenter.tamu.edu>  
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**Tierra Grande** (ISSN 1070-0234) is published quarterly by the Real Estate Center at Texas A&M University, College Station, Texas 77843-2115. Subscriptions are free to Texas real estate licensees. Other subscribers, \$20 per year. Views expressed are those of the authors and do not imply endorsement by the Real Estate Center, Mays Business School or Texas A&M University. The Texas A&M University System serves people of all ages, regardless of socioeconomic level, race, color, sex, religion, disability or national origin. Photography/Illustrations: JP Beato III, p. 1.



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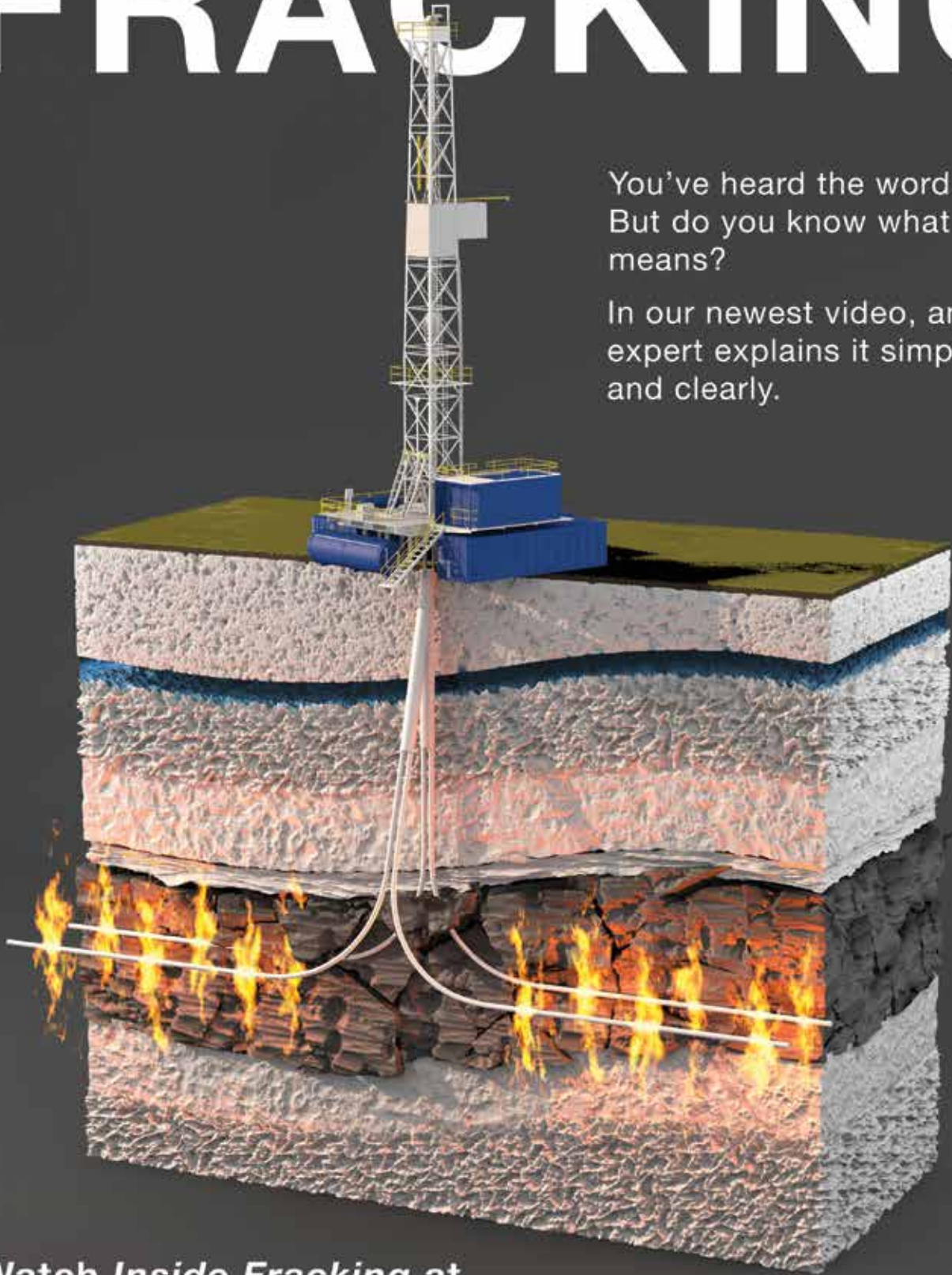
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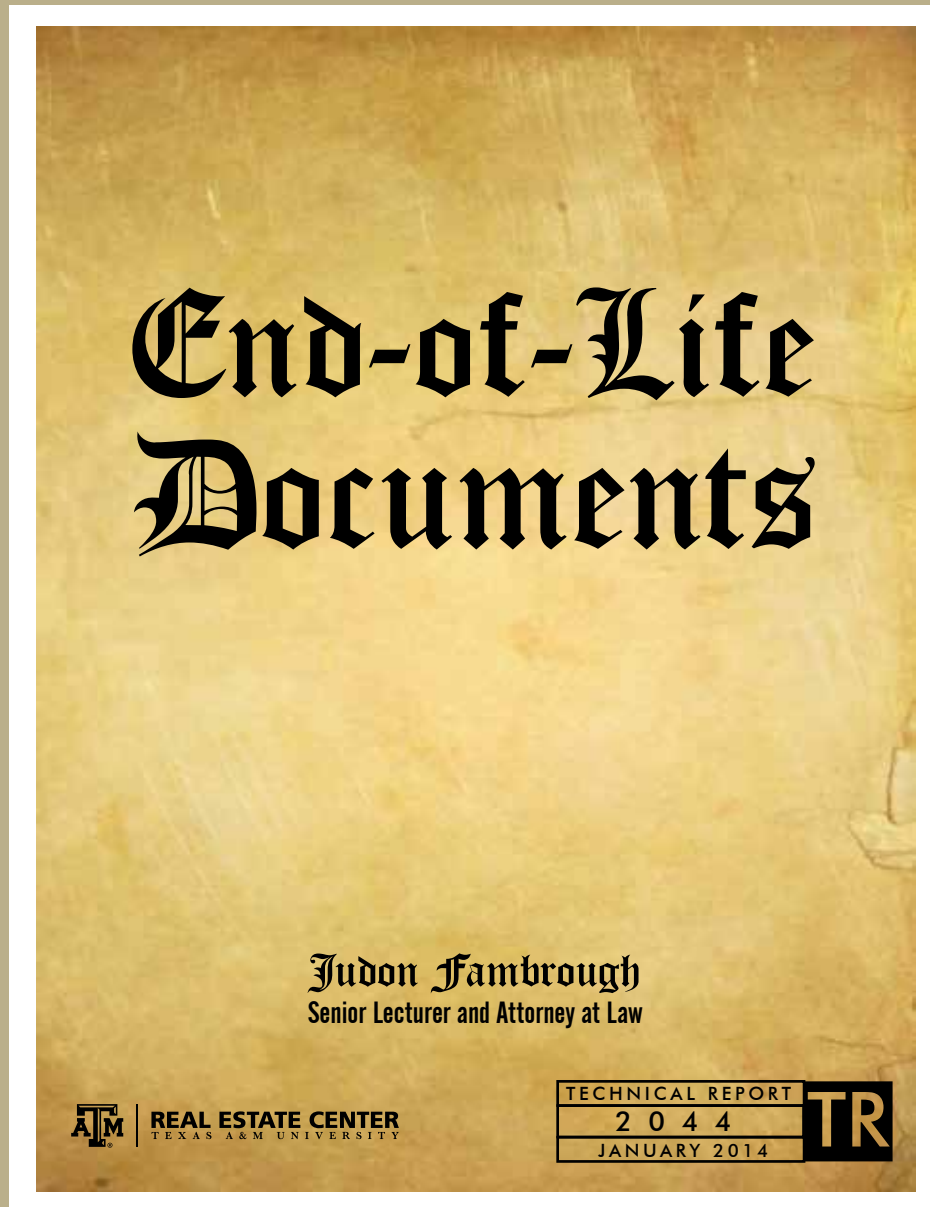


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