

Understanding North Carolina's Property Tax; Ensuring that your Real and Personal Property is not Overassessed*

Charles B. Neely, Jr.
Maupin Taylor & Ellis, P.A.
Raleigh, North Carolina

Introduction

All privately owned real and personal property (including intangible property) is subject to *ad valorem* taxation in North Carolina unless it is constitutionally exempted, or classified and excluded from taxation by statute.¹ Since the property tax annually generates city and county tax revenues in excess of \$4 billion, it is an important part of the tax structure in North Carolina.

Property statutorily classified and excluded from property taxation under authority of the North Carolina Constitution, art. V, § 2(2), is as diverse as the interest groups that have influenced the General Assembly to adopt their views of good public policy. Important classifications of excluded property include property used for environmental protection purposes, household furnishings, property belonging to a wide variety of non-profit organizations, intangible personal property other than leasehold interests in exempted real property, inventories of manufacturers, retailers and wholesalers, and some forms of computer software.² Other properties, most notably residential properties occupied by poor, elderly or disabled individuals and qualified agricultural, horticultural and forestland properties, are classified and assessed at reduced valuations.³

Under Article V, Sec. 2(3) of the North Carolina Constitution, property belonging to the State, counties and municipal corporations is exempt from taxation. The General Assembly is granted authority by the same section to exempt cemeteries and property held for educational, scientific, literary, cultural, charitable or religious purposes. The General Assembly has exercised that authority in G.S. § 105-278.1, *et seq.*

Most real and personal property is assessed locally by county assessors. The property of public service companies (railroads, electric power companies, telephone companies, etc.) is centrally assessed by the Department of Revenue each year. The assessment of both classes is governed by the Machinery Act.⁴

** This paper is an expanded version of an article, authored by Charles B. Neely, Jr. and Nancy S. Rendleman, which was published in the Winter 2001 edition, North Carolina State Bar Journal. An earlier version of this paper was presented to the May 2002 meeting of the Tax Sections of the North Carolina and South Carolina Bar Associations.*

¹ NC Const., art. V, §§ 2-3.

² N.C. GEN. STAT. § 105-275, *et seq.*

³ N.C. GEN. STAT. § 105-277, *et seq.*

⁴ N.C. GEN. STAT. § 105-271, *et seq.*

A. Listing and Assessment of Locally Assessed Real and Personal Property

1. Exemption or Exclusion Application Process

The application process for claiming exemption or exclusion from property taxes is set forth in the Machinery Act.⁵ Unless the statute provides to the contrary, an owner claiming exemption or exclusion must file an application on an annual basis during the listing period, which ends on January 31, unless extended.⁶ However, the exceptions seem largely to have swallowed the rule with regard to most of the excluded or exempt property which corporate taxpayers own. A careful examination of the statute and its many cross references is required in order to understand what property is eligible for exemption or exclusion and what the filing requirements are.

It is important to note that for certain types of excluded property such as that used for pollution control or recycling or resource recovery, once qualified for the exclusion, if additions, removals or improvements are made, the taxpayer must apply for the property to be excluded from taxation.⁷ The statute seems to imply that an application must be filed for all the property to be excluded – in other words the property already excluded as well as the new additions – but Department of Revenue staff advise that counties generally only require that the application for exclusion be filed for the new property.⁸

An application for exemption or exclusion may be filed after the close of the listing period upon a showing of “good cause.” However, an untimely application for exemption or exclusion may only be approved if the property tax is levied in the calendar year in which the untimely application is filed.⁹

2. Fair Market Value and Uniformity

All property subject to assessment must be assessed “at its true value in money,” or fair market value.¹⁰ The Machinery Act defines “true value” as “the price estimated in terms of money at which the property would change hands between a willing and financially able buyer and a willing seller, neither being under any compulsion to buy or to sell, and both having reasonable knowledge of all the uses to which the property is adapted and for which it is capable of being used.”¹¹

⁵ N.C. GEN. STAT. § 105-282.1.

⁶ N.C. GEN. STAT. § 105-307.

⁷ N.C. GEN. STAT. § 105-282.1(a)(3)a; *see also* N.C. GEN. STAT. § 105-275(8).

⁸ One complicating factor with regard to the exclusion of property devoted to pollution control, recycling or resource recovery relates to the requirement under N.C. GEN. STAT. § 105-275(8) that the Department of Environment and Natural Resources furnish a certificate to the tax supervisor stating that the property qualifies for the exclusion. DENR is frequently unable to provide such certificates within the time limits anticipated by the statute. In such a situation, the taxpayer should file a timely application for exclusion and supplement it with the certificate, once obtained.

⁹ N.C. GEN. STAT. § 105-282.1(a)(5); *see also* N.C. GEN. STAT. § 105-282.1(c).

¹⁰ N.C. GEN. STAT. 105-283.

¹¹ Id.

Further, under the North Carolina Constitution, all property in each county must be assessed uniformly.¹² As an example, it would constitute a violation of uniformity principles for the assessor to distinguish in assessment practice between property that has been sold and similar property that has not been sold. *See Edward Valves, Inc. v. Wake County.*¹³ In addition, N.C. GEN. STAT. § 105-284(a) imposes two uniformity requirements upon assessors: (1) that all property, real and personal, be assessed for taxation at its true value (or, in the case of agricultural, horticultural or forestland, at the value for which it is used, its “use value”) and (2) that all taxes imposed by counties and municipalities be levied uniformly on the assessments of fair market value.

The North Carolina Supreme Court has ruled that uniformity of assessment exists only with a uniform mode of assessment.¹⁴

3. Business Personal Property

The value of business personal property is determined annually as of January 1 based upon annual business personal property tax listings that must be filed by taxpayers in the county where the property is sited as of the first day of the year.¹⁵ In making assessments of personal property, the assessor must consider the various elements of value set forth in N.C. GEN. STAT. § 105-317.1, including replacement cost, sales price of similar property, age, physical condition, productivity and remaining life of the property, obsolescence, economic utility, and “any other factor” that may affect its value.

The Department of Revenue promulgates two publications that are heavily relied upon by assessors to determine fair market value of business personal property. These publications are the Personal Property Assessment Manual, used by the Department to teach the techniques of assessment of personal property, and the Cost Index and Depreciation Schedules, published by the Department on an annual basis. (See Exhibit A.)

Typically, counties determine the value of business personal property using the Cost Index and Depreciation Schedules promulgated by the Department of Revenue. They are designed to calculate fair market value by “trending” the installed historic cost of property by vintage year of acquisition to current reproduction cost and then depreciating the current reproduction cost through the use of depreciation tables based upon the estimated lives of classes of assets. Typically, subject to certain exceptions, assets are depreciated to a residual value of 25%. Once the asset reaches that level of depreciation, its value declines no further. While acceptable for mass appraisal purposes, the tables are generally not designed to account for external and functional obsolescence and unusual physical depreciation.

¹² NC Const., Art. V, Sec. 2; N.C. GEN. STAT. § 105-284.

¹³ *Edward Valves, Inc. v. Wake County*, 117 N.C. App. 484, 451 S.E.2d 641 (1995), 343 N.C. 426, 471 S.E.2d 342, stay granted, 339 N.C. 611, 454 S.E.2d 267 (1995), review granted, 340 N.C. 111, 456 S.E.2d 327 (1995), *aff'd as modified and remanded*, 343 N.C. 426, 471 S.E.2d 342 (1996), *reh'g denied*, 344 N.C. 444, 476 S.E.2d 115 (1996), *cert. denied*, 519 U.S. 1112, 117 S.C. 952 (1997).

¹⁴ *Hajoca Corp. v Clayton*, 277 NC 560, 569, 178 S.E.2d 481, 487 (1971).

¹⁵ N.C. GEN. STAT. § 105-285.

Personal property subject to significant external obsolescence—the textile industry is a good current example—is probably over-assessed under current tables. Likewise, the telecommunications manufacturing industry, telecommunications equipment, computer intensive manufacturing equipment and computers themselves are probably over-assessed under the current tables.

One opportunity to challenge an assessment that occasionally presents itself occurs when an industrial plant is sold with its installed machinery and equipment in place. Typically, the purchaser will pay a lump sum for the real estate and the installed personal property and then will allocate a portion of the purchase price to real estate, a portion to machinery and equipment, and a portion to other acquired assets, such as inventory and to intangibles, such as accounts receivable. Not infrequently, the purchase price of the real estate and buildings thereon and machinery and equipment will be significantly less than the assessed value of these assets.

Since personal property is assessed – and its fair market value determined – on an annual basis, the new property owner has the opportunity to raise the question of the assessed value of its business personal property as of January 1 of the following year by listing the allocated purchase price as its cost on the annual business personal property listing form. It may then argue that the last year’s sale represents the fair market value of the personal property. The Department of Revenue teaches assessors to apply the trending and depreciation schedules to the original historic cost of the property, i.e., the cost to the original owner, including the cost of freight, tax and installation.¹⁶ However, most business personal property listing forms used by counties make reference to the assets being listed at their installed purchase cost or words to that effect.

In some counties, notice of assessed value of business personal property will be mailed in the spring; in most counties, the taxpayer notice will be in the form of the annual tax bill, generally mailed in August. (See the discussion below in Section C as to how the timing of notice of assessed value affects taxpayer’s appeal remedies.)

The other major categories of assessable personal property consists of motor vehicles, boats, airplanes and mobile homes, all of which are assessable on an annual basis.

4. Real Property

Real property – land and the improvements thereto -- is valued on a countywide basis by the county tax assessor every eight years, unless the local taxing jurisdiction advances its revaluation schedule.¹⁷ Counties may advance the date of an octennial revaluation and many North Carolina counties are now revaluing property every four (4) years.

In appraising real property, the assessor must consider the elements set forth in N.C. GEN. STAT. § 105-317(a)(1) as to land (location, zoning, soil quality, mineral deposits, adaptability for

¹⁶ The Department of Revenue takes the position in its Personal Property Appraisal Manual that in the event of such a purchase, the assets should be reported at their original historic installed cost. See Page 6-20 of the Personal Property Appraisal Manual, September 2001.

¹⁷ N.C. GEN. STAT. § 105-285 and N.C. GEN. STAT. § 105-286.

different uses, past and future income, etc.) and those set forth in N.C. GEN. STAT. § 105-317(a)(2) as to buildings or other improvements (types of construction, age, replacement cost, cost, adaptability for uses as well as some of the factors listed in (a)(1)).

Each county, as part of its real estate revaluation process, must adopt a schedule of values, standards and rules before the revaluation begins.¹⁸ The schedule of values is, in essence, a “cookbook” to be followed by the assessor and his staff in conducting the revaluation. The schedule of values, which must be approved by the county commissioners before January 1 of the year for which they are to be applied, contains a relatively detailed set of “recipes” for the valuation of different types of real estate. The schedule of values establishes a valuation methodology for different types of real estate and is used to ensure the uniform assessment of real property.¹⁹

A particular taxpayer’s real property may be revalued between scheduled revaluation years if the value changes as a result of certain events, such as additions or expansions to a structure.²⁰ It is important to note that if the assessed value of real property is to be changed between scheduled revaluation years, as authorized by N.C. GEN. STAT. § 105-287, the changes must be made pursuant to the schedule of values adopted for the revaluation year governing the revaluation cycle. Following the schedule of values ensures that similar real property is valued under the same approach to value, using the same land costs and construction costs, as of the cycle revaluation date and helps ensure uniformity. Thus, in a county using an eight-year revaluation cycle, a new home constructed and sold in the sixth year and placed upon the assessment rolls when complete, as of January 1 of the seventh year, must be valued, not using the price for which it sold, but the construction costs and land costs in effect seven years earlier.

B. Appeals of Schedules of Value

Typically, the schedule of values is approved three to nine months before January 1 of the revaluation year. The assessor prepares the schedule of values, sometimes with the assistance of a consultant, submits them to the county board no less than 21 days before the hearing when they will be considered by the board, notice is published, the board adopts them, and notice of that action must be published in a paper of general circulation for four successive weeks thereafter.

Failure to give adequate notice of the adoption of the schedule of value is a denial of due process.²¹

A property owner who asserts that the schedules, standards, and rules are invalid may appeal from the order adopting the schedule of values to the Property Tax Commission within 30 days of the date when the order adopting them was first published.²²

¹⁸ N.C. GEN. STAT. § 105-317(b)(1) and (c)

¹⁹ N.C. GEN. STAT. § 105-317.

²⁰ N.C. GEN. STAT. § 105-287. See In re Allred, 351 NC 1, 519 S.E.2d 52 (1999) and In re Corbett, 355 N.C. 181, 558 S.E.2d 82 (2002).

²¹ In re McElwee, 304 N.C. 68, 79-81, 283 S.E.2d 115, 122-124 (1981)

²² N.C. GEN. STAT. § 105-317(c)(3)b.

Normally, this process does not present a problem because the schedules contain ranges broad enough to give the assessor significant leeway in making the assessment and not so narrow that if the taxpayer does not appeal the adoption of the schedule of values, he will have difficulty challenging an assessment made pursuant to the schedules. However, “the appeal procedure thus provided is the exclusive means for challenging the order adopting schedules, standards and rules for the octennial reappraisal of real property for taxation.”²³ (Emphasis added.) If the schedule for a particular property is drafted so tightly that its application will result in a higher than market valuation for a property, and the taxpayer does not appeal the adoption of the schedule of values, the taxpayer may well find itself without a remedy when it receives its notice of revalued assessment.

C. Appeals of Assessed Value

If a taxpayer concludes that his real property has been over-assessed, it is advisable to appeal the assessed value during the revaluation year, which, as noted above, occurs every 8 years unless the county has elected a 4-year cycle or otherwise advances the revaluation schedule.

Any relief granted will be effective for the year appealed and future years in the revaluation cycle. Appeals may, however, be taken after the revaluation year. See In re Property of Pine Raleigh Corp.²⁴ In such cases, the valuation of the property will be determined as of January 1 of the prior revaluation year, subject to the limited exceptions set forth in N.C. GEN. STAT. § 105-287 governing changes to the property thereafter. Any relief granted will not be retroactive.

Even though a property’s valuation has changed significantly since the general revaluation date, if the valuation change is not confined to something peculiar to the property, but is due to “economic changes affecting the county in general,” the property’s assessed value may not be changed until the next revaluation.²⁵

In the event that a taxpayer objects to the county tax assessor’s listing, appraisal or assessment of the taxpayer’s real property, the taxpayer may appeal to the county board of equalization and review.²⁶ (See Exhibit B for a form notice of appeal.) The board of equalization and review is comprised of the board of county commissioners unless the board of county commissioners has authorized a special board of equalization and review to hear property tax appeals.²⁷ County boards of equalization and review convene between the first Monday in April and the first Monday in May of each year to hear property tax appeals and must adjourn no later than July 1, (December 1 in revaluation years), or later under certain circumstances when the board has received a timely-filed appeal prior to its adjournment for the year.²⁸ In non-revaluation years it is not uncommon for boards to meet and adjourn on the same date. Since appeals to the county board

²³ Brock v. North Carolina Property Tax Commission, 290 N.C. 731, 228 S.E.2d 254 (1976).

²⁴ 258 N.C. 398, 128 S.E.2d 855 (1963)

²⁵ N.C. GEN. STAT. § 105-287(b). See Appeal of Hotel L’Europe, 116 N.C.App. 651, 652-654, 448 S.E.2d 865, 866 (1994), *disc. review denied*, 339 N.C. 612, 454 S.E.2d 252 (1995).

²⁶ N.C. GEN. STAT. § 105-322(g)(2).

²⁷ N.C. GEN. STAT. § 105-322(a).

²⁸ N.C. GEN. STAT. § 105-322(e).

must be filed prior to its adjournment,²⁹ in non-revaluation years a taxpayer would be well advised to file its appeal before the board convenes. The 2001 General Assembly expanded the powers and duties of boards of equalization and review by adding a new section, G.S. § 105-322(g)(5), which authorizes boards of equalization and review to continue to meet after adjournment to hear and decide discovery appeals, to hear and decide motor vehicle tax appeals, and to hear and decide appeals related to audits of property classified for present use valuation or under another classification for exclusion or exemption.

In revaluation years, some counties publish notice that the board will adjourn on June 30 or some other date, except for the purpose of hearing pending appeals. The purpose of this notice is to cut off the time for filing appeals as of the noticed date of adjournment, even though the board will continue to meet after that date to hear appeals previously filed. While the statutory scheme is ambiguous on this point,³⁰ a taxpayer should acquaint itself with the local rules to ensure that its appeal is timely filed. If a notice of the assessment of real or personal property is not delivered until after adjournment of the county board, the Property Tax Commission has held that an appeal is timely if filed before year-end on the grounds that failure to afford a hearing would constitute a denial of due process.

Traditionally, most counties did not provide notice of the annual assessed value of business personal property until tax bills were mailed, generally in August. Some counties provided notice of assessed value earlier in the year. The statutes were silent as to a taxpayer's appeal rights and the time limits and procedures for appealing the assessment of business personal property.

As noted above, the North Carolina Property Tax Commission has held that appeals were timely if filed with the county board of equalization and review, or if that board had adjourned, with the County Commissioners before year end.

The law pertaining to the appeal of business personal property assessments was clarified by the 2002 Session of the General Assembly. Beginning January 1, 2003, taxpayers must appeal the value, situs or taxability of the property within 30 days after the initial notice of value. If the assessor does not give a separate written notice of the value to the taxpayer at the taxpayer's last known address, then the tax bill will serve as the notice of value. Upon receipt of a timely appeal, the assessor must arrange a conference with the taxpayer to allow him to present any evidence or argument regarding the value, situs or taxability of the property. Within 30 days after the conference, the assessor must give written notice to the taxpayer of the assessor's final decision, unless the taxpayer signs an agreement accepting the value, situs or taxability of the property. If no agreement is reached, the taxpayer has 30 days from the notice to request a review by the local board of equalization and review, or, if it is not in session, by the county commissioners. The taxpayer will have 30 days to appeal a decision of the board of equalization and review or the county commissioners to the Property Tax Commission.³¹

Should a taxpayer receive a notice of assessed value and the taxpayer take no action to

²⁹ N.C. GEN. STAT. § 105-322(g)(2)(a).

³⁰ N.C. GEN. STAT. § 105-322(e) and (g)(2).

³¹ S.L. 2002-156.

appeal, it will be without a remedy to challenge that year's assessment of business personal property.

Upon appeal by a taxpayer that owns property in the county, the county board of equalization and review will review any decision of the county tax assessor with regard to the listing or appraisal of the taxpayer's property.³² The county board is authorized to examine and adjust the appraised value of the taxpayer's property and take other steps necessary to ensure that the property is appraised and taxed in conformity with statutory requirements.³³ If a taxpayer is "aggrieved" by the assessment of property he does not own, he may also appeal that assessed value.³⁴

County boards may increase or decrease the assessed value appealed. If the assessor discovers facts that lead him to believe that he under-assessed the property, he will undoubtedly ask the local board to increase his assessment.

Hearings before county boards are informal. Taxpayers may represent themselves, be represented by counsel and, in most counties, by family members, accountants or tax representatives. Witnesses are not sworn and the rules of evidence are not followed. Counties typically require non-lawyers representing property owners to produce a power of attorney before the appeal will be heard.

Although hearings on the appeals from county boards of equalization to the State Property Tax Commission (discussed below) are *de novo*, and although it often seems that hearings before local county boards are perfunctory, occasionally taxpayers will be able to obtain relief from county boards. The North Carolina Court of Appeals held in MAO/Pines Association, Ltd. v. New Hanover County Board of Equalization³⁵ that failure to reveal evidence of a factor (asbestos contamination in that case) allegedly affecting the true value of the taxpayer's property to the assessor or to the local board of equalization and review on a timely basis was sufficient basis for exclusion of evidence of that factor by the Property Tax Commission. Although the case was not conclusive on the point, in light of MAO/Pines, and in order to maintain a good working relationship with the county assessor, taxpayers would be well advised to apprise assessors of factors adversely affecting the value of their property during negotiations with the assessor and to advise the county board of equalization and review of these factors in appearances before these bodies.³⁶

D. ADiscovery@ Assessments and Appeal Procedure

If the county tax assessor determines that a taxpayer has not properly listed all real or personal property required to be listed, the assessor may make a discovery assessment of the

³² N.C. GEN. STAT. § 105-322(g).

³³ Id.

³⁴ See Brock v. North Carolina Property Tax Commission, *supra* note 23. See also In re Appeal of Whiteside Estates, Inc., 136 N.C.App. 360, 525 S.E.2d 196, *cert. denied*, 351 N.C. 473, 543 S.E.2d 511 (2000).

³⁵ 116 NC App. 551, 449 S.E.2d 196 (1994).

³⁶ But see also Brock v. North Carolina Property Tax Commission, *supra* note 23. "A county board of equalization and review operates in a very informal manner. No record is kept and usually little hard evidence exists to indicate the procedures followed. Therefore, appeals to the Property Tax Commission should not be dismissed on technical grounds, but only for clear noncompliance with statutory prerequisites."

unreported or under-reported property and charge penalties at the rate of 10% per year for the failure to report the property.³⁷ The assessor may make a discovery for the current year and the prior five (5) years.³⁸ Once the county tax assessor makes a discovery assessment, the assessor's listing and appraisal of the discovered property will become final unless the taxpayer files with the assessor a written exception to the discovery within thirty (30) days after receiving notice of the discovery.³⁹ Upon receipt of a timely written exception, the assessor will arrange a conference with the taxpayer to allow the taxpayer an opportunity to present evidence and arguments regarding the discovery.⁴⁰ Within fifteen (15) days of the conference, the assessor must give written notice of his final decision to the taxpayer.⁴¹ The taxpayer then has fifteen (15) days from the date of the notice to appeal to the county board of equalization and review or, if the board of equalization and review is not in session, to the county board of commissioners.⁴²

In recent years, many counties have used the services of contract auditors who frequently work on a contingent fee basis. This procedure, while objectionable to taxpayers confronted by an auditor who will be paid based upon his success in defending his discovery assessment recommendations to the assessor, has been approved by the North Carolina Supreme Court.⁴³

While the assessor has authority to determine the value of discovered property, he does not have authority to waive the assessment of penalties.

The county board of commissioners is authorized to compromise, settle, or adjust the county's claim for taxes arising from a discovery assessment, including the penalties associated therewith.⁴⁴ This power may be delegated by the board of commissioners to the board of equalization and review or to any special board established by local act.

This power to compromise discovery assessments constitutes an exception to the general rule that tax assessments may not be compromised without significant peril in the way of personal liability to the county commissioners.⁴⁵ However, to qualify for the compromise provisions, the taxpayer will generally have to forego its appeal remedies to the Property Tax Commission, allow the assessment to become final and hope that it will be able to negotiate a compromise of the penalties and/or tax with the county commission. (Theoretically, this relief might also be available after trial before the Property Tax Commission, but experience indicates that county commissioners will be loath to compromise after incurring the expense of a trial to vindicate the county's assessment.)

³⁷ N.C. GEN. STAT. § 105-312.

³⁸ N.C. GEN. STAT. § 105-312(f) and (g).

³⁹ N.C. GEN. STAT. § 105-312(d).

⁴⁰ Id.

⁴¹ Id.

⁴² Id.

⁴³ In re Appeal of Philip Morris U.S.A., 335 NC 227, 436 S.E.2d 828 (1993), *reh'g denied*, 335 NC 566, 441 S.E.2d 118, *cert. denied*, 512 US 1228, 114 S. Ct. 2726 (1994).

⁴⁴ N.C. GEN. STAT. § 105-312(k)

⁴⁵ N.C. GEN. STAT. § 105-380.

E. Listing and Assessment of Centrally Assessed Property

The property of centrally assessed public service companies (PSC) is annually assessed by the Department of Revenue.⁴⁶ The values of system property (the realty and personalty used in public service activities, whether in or out of North Carolina) are in most instances determined based upon the unit value of the entire PSC and are then apportioned to North Carolina based upon the ratio that the taxpayer's property, business or mileage in North Carolina bears to its total national property, business, or mileage.⁴⁷ The North Carolina apportioned value is then allocated by the Department among local taxing units based upon statutory formulas for each PSC.⁴⁸

The value of non-system PSC property (realty and personalty not used in public service activities) is appraised by the Department and certified to the taxing units in which the properties are situated.⁴⁹

The valuations of system and non-system real and personal property certified by the Department to local taxing units are then assessed locally at the same rates of tax levied against other property in the local taxing jurisdictions.

To prevent discrimination in taxation against centrally assessed taxpayers in favor of local taxpayers, and to cure the discrimination inherent in a system in which locally assessed real property is revalued octennially and PSC property is assessed annually, the General Assembly enacted remedial relief.⁵⁰ In simplified terms, the appraised value of PSC system property is adjusted by applying to the amount allocated to each county a percentage which reflects the level of assessment of other property in the county compared to its fair market value based on real estate sales assessment ratio studies conducted in the revaluation year and the fourth and seventh years thereafter, if the sales assessment ratio studies show a level of real estate assessment in the county below 90%.⁵¹ This procedure is designed to correct for the effects of inflation and demand on the purchase price of real property over the reassessment cycle, which generally results in real property being assessed at less than fair market value in later years of the cycle.

Valuation, apportionment and equalization decisions of the Department of Revenue relative to PSC property are subject to appeal by the taxpayer to the Property Tax Commission.⁵²

F. Appeals to Property Tax Commission

⁴⁶ N.C. GEN. STAT. § 105-335, *et seq.*

⁴⁷ N.C. GEN. STAT. § 105-337.

⁴⁸ N.C. GEN. STAT. § 105-338.

⁴⁹ N.C. GEN. STAT. § 105-339.

⁵⁰ N.C. GEN. STAT. § 105-284(b).

⁵¹ Certain class 1 railroads have won injunctive relief in federal court entitling them to relief from discrimination under 49 USC §11503 (the "4R Act") if the level of assessment of real estate is 95% or less. This relief is afforded annually.

⁵² N.C. GEN. STAT. § 105-342; N.C. GEN. STAT. § 105-284(c).

1. Procedure

If a taxpayer objects to the resolution of his locally assessed property tax appeal by the county board of equalization and review or board of county commissioners, or if a public service company objects to a valuation or apportionment decision by the Department of Revenue, the taxpayer may appeal to the state Property Tax Commission.⁵³ (See Exhibit C for a form notice of appeal.) The county assessor may not appeal an adverse ruling of the county board.⁵⁴ Three of the five members of the Commission are appointed by the Governor, one member is appointed by the Speaker of the North Carolina House of Representatives, and one member is appointed by the President Pro Tempore of the North Carolina Senate.⁵⁵

For locally assessed property, written notice of appeal to the Commission must be filed within thirty (30) days after the date that the county board of equalization and review mails a notice of its decision to the property owner.⁵⁶ An appeal by a PSC to the Commission must be filed within 20 days after the date that the Department of Revenue mails notice of its tentative appraisal and apportionment.⁵⁷ Challenges to equalization decisions must be given within 30 days after the mailing of the Department's notice.⁵⁸ The Commission promulgates rules governing its procedures, which may be found at N.C. Admin. Code tit. 17, r. 11.

Under the Commission procedures, the taxpayer must timely request a hearing. This is accomplished by the filing of Commission Form AV14, Application for Hearing, which is mailed to the taxpayer after the appeal is filed. It must be filed within 30 days of the date it is mailed. According to Commission rules, only taxpayers appearing *pro se* or attorneys licensed to practice law in North Carolina may file appeals to the Commission or otherwise appear before that body.⁵⁹ After an appeal is filed, the staff of the Property Tax Division of the Department of Revenue will consult with both the taxpayer and the county in an attempt to mediate the appeal informally. The staff is knowledgeable and helpful and their efforts are frequently successful.

Although the Rules of Civil Procedure do not apply to proceedings before the Commission, the rules pertaining to discovery have been adopted and are available for use by the parties.⁶⁰ The Commission encourages the use of informal discovery. In addition, the Commission has the authority to issue subpoenas.⁶¹

⁵³ N.C. GEN. STAT. § 105-290; N.C. GEN. STAT. § 105-342(b).

⁵⁴ N.C. GEN. STAT. § 105-290(b); In re Appeal of Forsyth County, 104 N.C.App. 635, 410 S.E.2d 533 (1991), *disc. rev. denied*, 330 N.C. 851, 413 S.E.2d 551 (1992).; In re Moses H. Cone Memorial Hospital, 113 N.C.App. 562, 439 S.E.2d 778 (1994), *aff'd in part, cert. improvidently granted in part*, 340 N.C. 93, 455 S.E.2d 431 (1995).

⁵⁵ N.C. GEN. STAT. § 105-288.

⁵⁶ N.C. GEN. STAT. § 105-290(e). See In re Appeal of Intermedia Communications, Inc., 144 NC App. 424, 548 S.E.2d 562 (2001) (allowing an appeal to be filed by fax).

⁵⁷ N.C. GEN. STAT. § 105-342(b).

⁵⁸ N.C. GEN. STAT. § 105-284(c).

⁵⁹ N.C. ADMIN. CODE tit. 17, r. 11.0216.

⁶⁰ N.C. ADMIN. CODE tit. 17, r. 11.0218.

⁶¹ N.C. GEN. STAT. § 105-290(d).

2. Hearings

The full Commission may hear the taxpayer=s appeal or, in rare instances, it may designate one or more Commission members or Department employees to hear the appeal and issue a proposed decision which may then be accepted or rejected by the full Commission after review of the record and any written arguments of the parties.⁶² Typically, the Commission meets monthly, usually in Raleigh. Hearings before the Commission are *de novo*⁶³ and are conducted under the North Carolina Rules of Evidence.⁶⁴

The duties of the [Property Tax] Commission are quasi-judicial in nature and require the exercise of judgment and discretion.⁶⁵ The Commission has the duty “to determine the weight and sufficiency of the evidence and the credibility of the witnesses, to draw inferences from the facts, and to appraise conflicting and circumstantial evidence.”⁶⁶

An *ad valorem* tax assessment is presumed correct.⁶⁷ This presumption is only one of fact and is, therefore, rebuttable. This presumption may be rebutted by material, substantial, and competent evidence that tends to show that either an arbitrary or an illegal method of valuation was used and that the assessment substantially exceeded the true value in money of the property.⁶⁸ It is not enough for the taxpayer to show that the method used by the assessor was wrong; the taxpayer must also show that the result of the valuation is substantially greater than the true value in money of the property assessed.⁶⁹ The converse is also true – the taxpayer must not only prove that the value is substantially in excess of true value, he must prove that the assessment was arbitrary or illegal.⁷⁰ The good faith of tax assessors and the validity of their actions are presumed. The taxpayer bears the burden of showing that the assessment was erroneous.⁷¹

“When a taxpayer has rebutted the presumption of regularity in favor of the county . . . the burden then shifts to the county to demonstrate to the Property Tax Commission that the values determined in the revaluation process were not substantially higher than that called for by the statutory formula, and the county must demonstrate the reasonableness of its valuation by ‘competent, material and substantial evidence.’”⁷² The Supreme Court observed in In Re Southern Railway⁷³ that when the taxpayer offered evidence that the appraisal methods used by the assessing

⁶² N.C. GEN. STAT. § 105-290(b).

⁶³ Appeal of Forestry Foundation, 35 N.C.App. 414, 425, 242 S.E.2d 492, 499 (1978), *aff’d*, 296 N.C. 330, 250 S.E.2d 236 (1979).

⁶⁴ N.C. GEN. STAT. 8C-1.

⁶⁵ Albemarle Electric Membership Corp., 282 N.C. 402, 409, 192 S.E.2d 811, 816 (1972).

⁶⁶ In re McElwee, *supra* note 21 at 87, 283 S.E.2d at 126-27.

⁶⁷ In re Appeal of AMP, Inc., 287 N.C. 547, 561, 215 S.E.2d 752, 761 (1975).

⁶⁸ Id. at 563, 215 S.E.2d at 762.

⁶⁹ Id.

⁷⁰ Id.

⁷¹ In re McElwee, *supra* note 21 at 75, 283 S.E.2d at 120.

⁷² In re McElwee, *supra* note 21 at 86-87, 283 S.E.2d at 126-7 (1981).

⁷³ In re Appeal of Southern Railway Co., 313 N.C. 177, 328 S.E.2d 235 (1985).

authority would not produce true values for the taxpayer and that the values actually produced by these methods were substantially in excess of true value, they rebutted the presumption of correctness. “The burden of going forward with evidence and of persuasion that its methods would in fact produce true values then rested with the [assessing authority] and it became the Commission’s duty to hear the evidence of both sides, to determine its weight and sufficiency and the credibility of witnesses, to draw inferences, and to appraise conflicting and circumstantial evidence, all in order to determine whether the [assessing authority] met its burden.”

“An illegal appraisal method is one which will not result in true value as that term is used in N.C. GEN. STAT. § 105-283 and, for public service companies, in N.C. GEN. STAT. § 105-335.”⁷⁴ The Supreme Court held in AMP that the use of book value as a *per se* indicator of fair market value was illegal.⁷⁵ An appraisal method contrary to the Machinery Act is an illegal method of valuation.⁷⁶ The Supreme Court further observed in McElwee that the use of comparable sales constituted an illegal method of valuation when the “comparable” land which had been sold was not shown to be used for the same purposes as the land being valued.⁷⁷ “An illegal appraisal method is one which will not result in ‘true value’ as that term is used in [G.S. § 105-283]”⁷⁸

The use of valuation guides without consideration of the condition of the article being valued has been held to be an arbitrary method of valuation.⁷⁹ A revaluation process conducted 2½ years before the effective date of the appraisal and under a short time frame (2 months) is “plainly arbitrary.”⁸⁰ Failure to take restraints on alienation into account in assessing real property was found to be arbitrary.⁸¹ Averaging of comparable sales and omitting other comparable sales from the average without apparent analysis of the comparable sales was found to be arbitrary; assessing real property based on a figure per front foot without considering suitability of tract for building was found to be arbitrary.⁸²

Hearings before the Commission on the assessed valuation of properties typically involve battles between expert witnesses, including appraisers, cost estimators and engineers, and generally turn on questions of the highest and best use of the property, the determination of obsolescence and depreciation under the cost approach to value, the comparability of “comparable sales” under the market data approach to value, and calculations of net operating income and its appropriate capitalization, or use of the discounted cash flow method, under the income approach to value.

⁷⁴ Southern Railway Co., *supra* note 73 at 181, 328 S.E.2d at 239.

⁷⁵ AMP, *supra* note 67 at 563-65, 215 S.E.2d at 762-63.

⁷⁶ Id.

⁷⁷ In re McElwee, *supra* note 21 at 88-91, 283 S.E.2d at 127-29.

⁷⁸ Appeal of Colonial Pipeline, 318 N.C. 224, 236, 347 S.E.2d 382, 389 (1986).

⁷⁹ In re Carolina Quality Block Co., 270 N.C. 765, 155 S.E.2d 263 (1967).

⁸⁰ In re McElwee, *supra* note 21 at 82-84, 283 S.E.2d at 124-125.

⁸¹ In re Appeal of Perry-Griffin Foundation, 108 N.C. App. 383, 424 S.E.2d 212, *disc. rev. den’d*, 333 N.C. 538, 429 S.E.2d 561 (1993).

⁸² In re Appeal of Boos, 95 N.C.App. 386, 382 S.E.2d 769 (1989).

Appraisers will typically consider all of the three approaches to determining fair market value – cost, income, and comparable sales – and, depending upon the availability of data, will use one or more of these methods, frequently using all three.

Although theoretically all three approaches to the determination of market value should yield approximately the same number, in practice they generally do not, leaving the appraiser to reconcile the approaches he used and to determine which approach he must most heavily rely upon.

Battles are frequently waged before the Property Tax Commission and the appellate courts on the propriety of particular valuation methods.

Our courts have held that the income approach is most appropriate for the valuation of investment properties like mall anchor stores⁸³ and super regional malls.⁸⁴ In using the income approach to value properties, it is important to note that North Carolina is a “market rents” state and not a “contract rents” state; for property tax purposes, the market rents of comparable properties are used and not the properties’ actual contract rents, although an appraiser may determine, based upon his survey of the market, that the properties’ actual rents reflect the market.⁸⁵

Two recent cases have clouded the issue in North Carolina as to just what the “market” is – Belk-Broome⁸⁶ and Greens of Pine Glen, Ltd.⁸⁷ In Belk-Broome, the Court of Appeals held that in valuing mall anchor stores, the assessor’s reliance on the cost approach was inappropriate because the income produced by market rents for mall anchor stores should be the primary measure of value. The court noted that mall anchor stores have a special, more restricted market due to the existence of operating agreements that provide lower rents in the form of a subsidy by the mall developers to the department store. Even though the rents are lower for mall anchors, “The operating agreement is an integral part of that market . . . The property must be valued according to that market . . . The County and Commission must take the property as it finds it.”⁸⁸

In Greens of Pine Glen (on appeal to the North Carolina Supreme Court), the Court of Appeals, considering the valuation of low income subsidized rental apartments (“Section 42 housing”), held that the replacement cost method used by the assessor was inappropriate given the restrictions on the income stream paid to the owner. In distinguishing North Carolina’s market rent cases, the court held that an encumbrance on low income housing is “more akin to the uniform restrictions placed on anchor department stores in Belk-Broome” than to an unfavorable lease on a property.⁸⁹

⁸³ In re Appeal of Belk-Broome Co., 119 N.C.App. 470, 458 S.E.2d 921 (1995).

⁸⁴ In re Winston-Salem Joint Venture, 144 N.C.App. 706, 551 S.E.2d 556, *disc. review denied*, 354 N.C. 217, 555 S.E.2d 277 (2001).

⁸⁵ In re Greensboro Office Partnership, 72 N.C.App. 635, 325 S.E.2d 24, *cert. denied*, 313 N.C. 601, 330 S.E.2d 610 (1985); In re Pine Raleigh Corp., 258 N.C. 398, 128 S.E.2d 855 (1963).

⁸⁶ In re Appeal of Belk-Broome Co., *supra* note 83.

⁸⁷ In re Greens of Pine Glen Ltd. v. Durham County Bd. of Equalization & Review, 555 S.E.2d 612 (N.C. Ct. App. 2001), *pet. for disc. review allowed*, 355 N.C. 286 (2002).

⁸⁸ In re Appeal of Belk-Broome Co., *supra* note 83 at 478-480, 458 S.E.2d at 926-27.

⁸⁹ In re Greens of Pine Glen Ltd., *supra* note 87.

Our Supreme Court has held that the income approach is appropriate for the valuation of property assessed at its present use.⁹⁰

Our courts have indicated that, “The cost approach is better suited for valuing specialty property or newly developed property . . .”⁹¹

The comparable sales approach seems to be particularly useful for the valuation of raw land and single family residences, and when market comparables are available, for other types of property, such as apartment complexes, office buildings, or retail uses,⁹² keeping in mind the court’s preference for the income approach for investment grade properties.

Industrial plants, particularly older ones, present significant appraisal challenges. Rental income data is rarely available since these properties are generally owner occupied. Many plants have significant physical, functional and external obsolescence, providing for subjective adjustments to the replacement cost new. Although comparable sales are frequently available, even for large plants, the assessor invariably contends that the “dangling wire plants” which have been sold (plants from which all the machinery and equipment have been removed) are not comparable to plants in economically productive use.

Similarly, the appraisal of machinery and equipment presents significant obstacles. Since this equipment is generally not rented, it is difficult to develop an income stream to be capitalized. Machinery and equipment, once shut down and sold from a plant, frequently goes for pennies on the dollar. The cost approach, with proper consideration given to physical depreciation and all forms of obsolescence, seems to be most generally accepted as the best approach. Quantification of obsolescence, however, is not easily accomplished and appraisers who really know what they are doing are pearls of great price.

Issues frequently confronted in the appraisal of machinery and equipment include

- Ghost assets – assets that have been disposed of but not removed from the company’s fixed asset records, or retained in the plant but with no hope of resurrection, frequently having been cannibalized for use with other equipment.
- Idle equipment – usable equipment, but not in use due to lack of product demand.
- Construction in process and new construction – how to value additions to an obsolescent plant.
- Distinguishing between realty and personalty, when the personalty is often permanently affixed to the realty.

⁹⁰ In re McElwee, *supra* note 21 at 92, 283 S.E.2d at 130.

⁹¹ In re Appeal of Belk-Broome Co., *supra* note 83 at 474, 458 S.E.2d at 924.

⁹² In ascertaining market value, sales of comparable property are the most reliable indicators of value. United States v. 100.80 Acres of Land, 657 F. Supp. 269, 274 (M.D.N.C. 1987); City of Statesville v. Cloaninger, 106 N.C. App. 10, 16, 415 S.E.2d 111, 115 (1992), *disc. review denied*, 331 N.C. 553, 418 S.E.2d 664 (1992).

As a general rule, the Property Tax Commission staff, and most appraisers, tend to regard the equipment installed in the plant for plant lighting, air handling and plumbing for human comfort, distribution wiring, etc., to be part of the real estate, while equipment installed for purposes of the manufacturing process to be conducted within the plant to be personalty.⁹³

Finally, after the parties have introduced their evidence, the Commission “shall make findings of fact and conclusions of law and issue an appropriate order” based on evidence considered at the hearing.⁹⁴

The Property Tax Commission has no authority to rule on constitutional issues. These must be raised and preserved for the appellate courts.⁹⁵

G. Judicial Review

Any party aggrieved by a final order or decision of the Commission may appeal to the North Carolina Court of Appeals by filing with the Commission within thirty (30) days after entry of the final decision or order being appealed a notice of appeal and a statement of alleged errors made by the Commission in its decision.⁹⁶ The appealing party must also serve notice of the appeal on all other parties to the action and perfect the appeal in the Court of Appeals in accordance with the Rules of Appellate Procedure. Either the taxpayer or the taxing jurisdiction may appeal the decision of the Court of Appeals to the North Carolina Supreme Court as provided in the Rules of Appellate Procedure.

G.S. § 105-345.2(b) establishes the standard of review to be applied by this Court upon an appeal of a decision of the Commission:

The court may affirm or reverse the decision of the Commission, declare the same null and void, or remand the case for further proceedings; or it may reverse or modify the decision if the substantial rights of the appellants have been prejudiced because the Commission’s findings, inferences, conclusions, or decisions are:

- (1) In violation of constitutional provisions; or
- (2) In excess of statutory authority or jurisdiction of the Commission; or
- (3) Made upon unlawful proceedings; or
- (4) Affected by other errors of law; or
- (5) Unsupported by competent, material and substantial evidence in view of the entire record as submitted; or

⁹³ See Personal Property Assessment Manual, September, 2001, p. 2-2. The Manual contains a useful checklist classifying selected items as realty or personalty.

⁹⁴ N.C. GEN. STAT. § 105-290(b)(2).

⁹⁵ Gulf Oil Corp. v. Clayton, 267 N.C. 15, 147 S.E.2d 522 (1966); Great American Insurance Company v. Gold, 254 N.C. 168, 118 S.E.2d 792 (1961), *overruled on other grounds*, Smith v. State, 289 N.C. 303, 222 S.E.2d 412 (1976).

⁹⁶ N.C. GEN. STAT. § 105-345.

(6) Arbitrary or capricious.

G.S. § 105-345.2(c) requires: “(I)n making the foregoing determinations, the court shall review the whole record . . . and due account shall be taken of the rule of prejudicial error.” Under a “whole record” analysis, the reviewing court may not

replace the [Commission’s] judgment as between two reasonably conflicting views, even though the court could justifiably have reached a different result had the matter been before it *de novo* (citation omitted). On the other hand the “whole record” rule requires the court, in determining the substantiality of evidence supporting the [Commission’s] decision, to take into account whatever in the record fairly detracts from the weight of the [Commission’s] evidence. Under the whole evidence rule, the court may not consider the evidence which in and of itself justifies the [Commission’s] result, without taking into account the contradictory evidence or evidence from which conflicting inferences could be drawn (citation omitted).⁹⁷

However, “it is clear that no court of the General Courts of Justice can weigh the evidence presented to the [Commission] and substitute its evaluation of the evidence for that of the [Commission].”⁹⁸ If the Commission’s decision, considered in the light of the foregoing rules, is supported by substantial evidence, it cannot be overturned.⁹⁹ Substantial evidence means more than a scintilla of evidence or such evidence as a reasonable person might accept as adequate.¹⁰⁰

H. Action Brought Directly in Superior Court

A taxpayer may, in certain circumstances, bypass administrative appeals of its property tax assessment and seek judicial review in a state trial court by filing with the city or county that imposed the tax a demand for the release of any tax assessed but not paid or, in the event that the taxpayer has already paid the tax, a claim for refund.¹⁰¹ This procedure is available only in instances where the taxpayer alleges that the property tax was imposed through clerical error, an illegal tax, or a tax levied for an illegal purpose. It would not, for instance, apply where the taxpayer challenges the appraised value of its property.¹⁰²

If the taxing body does not grant the requested release or refund within ninety (90) days after receipt of the request, the taxpayer may file suit against the taxing body for the tax amount

⁹⁷In re McElwee, *supra* note 21 (citing Thompson v. Wake County Board of Education, 292 N.C. 406, 233 S.E.2d 538 (1977)).

⁹⁸AMP, *supra* note 67.

⁹⁹In re Appeal of Interstate Income Fund I, 126 N.C.App. 162, 484 S.E.2d 450 (1997); In re Appeal of Perry-Griffin Foundation, *supra* note 81.

¹⁰⁰In re Appeal of General Tire, Inc., 102 N.C. App. 38, 40, 401 S.E.2d 391, 393 (1991) (Substantial evidence supported the Commission’s decision).

¹⁰¹N.C. GEN. STAT. § 105-381.

¹⁰²Edward Valves, Inc., *supra* note 13 at 489, 451 S.E.2d at 645 (“If a taxpayer disagrees with a county’s valuation of its property, the taxpayer must pursue and exhaust its administrative remedies before resorting to the courts...Questions concerning valuation which are first presented directly to the courts are properly dismissed.” (citations omitted)).

claimed.¹⁰³ If the taxpayer sought a release from an unpaid property tax and did not receive the requested release of the tax from the taxing body, the taxpayer must first pay the tax due before filing suit. The taxpayer in that circumstance may file suit within three (3) years after payment of the tax. A taxpayer filing suit after the 90-day period for approval of his refund claim has passed must file suit within three (3) years after the date when the governing body was required to act on the taxpayer's refund claim.¹⁰⁴

Conclusion

The assessment and appeals procedure set forth in the Machinery Act are comprehensive. Failure to follow its procedures may result in dismissal of a taxpayer's appeal but an understanding of them will allow attorneys to assist their clients in resolving property tax disputes and reduce their tax assessments in appropriate cases.

Charles B. Neely, Jr. is engaged in the practice of state and local tax law with Maupin Taylor and Ellis, P.A., Raleigh, N.C.

¹⁰³ N.C. GEN. STAT. § 105-381(c).

¹⁰⁴ Id.