Webinar 3: Individual & Commercial Personal Property Assessments

Hosted by Wayne Miller, Professor at the University of Arkansas System Division of Agriculture and presented by Steve Sutterfield, Personal Property Manager at the Arkansas Assessment Coordination Department on July 20, 2018

[Wayne Miller] Good morning and welcome to the Individual and Commercial Personal Property Assessment webinar. I'm Wayne Miller, Professor with the Community & Economic Development program at the University of Arkansas System Division of Agriculture.

And today's webinar is a third in a series of six webinars on property assessments in Arkansas. This is part of our local government program. And it's in collaboration with the Arkansas Assessment Coordination Department and the tax division of the Arkansas Public Service Commission.

As in the previous seminars, we want to emphasize a little bit, the importance of the property tax. You know the property tax is a local tax supporting local services. Every dollar the property tax generates goes into your K through 12 schools, your county and cities, roads and bridges. Your police and fire departments, your libraries and many more services such as agriculture, health services, recreation programs and facilities.

And so since we all benefit from the property tax, which supports these local services, we think it's important to understand how the properties are assessed, and what properties are assessed. And most of us own at least at one vehicle: a car, truck, motorcycle or RV. So we all pay their personal property tax. But did you know that businesses and farms also pay a personal property tax?

So, fortunately, today we have with us Steve Sutterfield, who is the business and personal property manager with the Arkansas Assessment Coordination Department with the Arkansas Assessment Coordination Department.

Steve has many years of experience with property assessments, both in the public and private sectors, working with county governments, state agencies and the private industry since 1982. Steve has developed course materials and valuation manuals. He's published papers, and he's also been an invited speaker for many estate and international conferences, seminars and meetings. He has too many awards to recognize all of them today, but just to mention a couple, he's been designated as the Personal Property Specialist with the International Association of

Assessing Officers, and he was, I think, their member of the year in 1993. He has also received many state recognitions and awards as well. But, he is an Arkansas certified general appraiser and appraisal manager, so he has definitely a property assessment expert and we are glad to have you with us today, Steve, and we look forward to your presentation.

[Steve] Thank you, I'm delighted to be here. I do have to add real quick that I have always heard the shorter the introduction, the easier it is to live up to it, so I'll do my best.

We're going to talk about personal property generally, and the best way to identify the various types. The statue itself, the primary statute, 26-3-201, that's Arkansas Code Annotated, says that all property, whether real or personal, in this state shall be subject to taxation. Such property shall be entered on the list of taxable property for that purpose.

Now property is either tangible or intangible. Tangible, of course, meaning it has a physical presence. Intangible means it's simply representative of ownership. That's money stocks, bonds, things so that sort. The Constitution of Arkansas exempts intangible property from assessment and taxation.

So we're going to talk about tangible property and that's going to cover all real and most personal [property]. Real Property is land and improvements on the land. Pretty simple. This property is automatically reviewed on a cyclical basis by the assessor. The value is updated over, right now, we are on five year periods, I believe, in pretty much every county.

Personal property is defined as every tangible thing being the subject of ownership, and not forming a part of any parcel of real property as defined. It's defined by exception, if it ain't real, it must be personal.

This chart I believe came from you guys. This what someone told me, but I saw it in an earlier presentation. I really liked this. I work in personal property and I wasn't aware how much we have statewide. If you add up the total of automobiles, the business personal and the miscellaneous becomes in just under $10 billion. I think about $9.9 billion. And it's equivalent, [or] pretty close, to the value of all the land in the state. That doesn't include the improvements on real estate, but it's no small amount.

And you'll see that the autos, and that includes all the various types of vehicles. We'll get into that in a minute. But that amount is almost equivalent to the amount of the business sales. I love this chart.

Personal property is assessed every year by the assessor. It's kind of like, we go through a five year cycle on reappraising real property. Well, we have to revalue all personal property every single year. And the value of all that is based on what it's worth, January 1. Now it's to be listed with the assessor no later than May 31st, by the owner, this is not done automatically and failure to do it in a timely manner can result in late assessment penalty of 10%. You need to check with the local assessor--it's possible that you can assess online.

And all counties can take assessments by telephone. Once they have assessed you the first time in the office. They need a signature on a form at some point, but beyond that more and more counties each year coming to where they have the capability of let you assess online.

Now I like to break property into tax according ownership, and we'll start with the property of individuals. That was that big pie piece a while ago that said automobiles. It does consist mostly of vehicles. Pretty general: automobiles; light, medium, heavy duty trucks; boats; motors; trailers; RVs (recreational vehicles); motor cycles and ATVS; and aircraft. There are about 3,000 aircraft in Arkansas. We track all of those and help assessors to value them.

And then I like to talk about one that's might be a little closer to your interests, and that's farm equipment. Farm equipment is kind of a gray area. We're going to have farm trailers, you know, general purpose utility type trailers, stock trailers, general farm equipment and attachments, and livestock.

Maybe a good rule of thumb is that if you're going to be using it on the road, if it has to have a tag, it's going to have to be assessed, you're going to need to list it with the assessor, but a lot of this stuff moves into what I consider commercial property. Little note here about the above referred to hobby farms. I don't know too many people at farm for the fun of it, maybe for the love of it, but most of you who farm are doing it to try to make a living. And your personal property used for that purpose will be assessed as commercial personal property, just like the equipment in a business or something.

I always, when I get this, I can't help thinking that I spent all my teenage years in the summer hauling hay, they hadn't invented round bailers yet, and if my dad was hobby farming I'm going to have to go back and some words with him. I wish I had taken up fishing or something.

Hobby farms, seriously, we're going to mention here in a minute, household property is not taxed. If someone has a couple acres of garden and maybe a little 12-15 horse (power) tractor they use on that, we're not considering that commercial production. So there are going to be instances where farmer equipment won't even be assessed, but if it's used to produce income, it really becomes commercial property. And right here, property used in or about the household is exempt, if not used to produce income.

Some of you may recall, years ago, we used to assess household property at a rate per room, they would ask you how many rooms of furniture you had when you went to assess. That's been gone for several years, but it can't be used to produce income. It's not uncommon to see a home business someone will have an office out of their home. I had a call a while back to buy the lady that made cupcakes and so advertised on the internet, everything. The assessor assessed her kitchen as commercial property, and rightly so.

So, that moves us into commercial or what we call business personal property. Businesses typically are either service businesses or retail; that is, they provide a service like selling insurance going to the doctor or whatever, or they're retail. Retailers own inventory for the purpose of selling. Resale.

So, retail businesses produce income through the sale of inventory while service businesses do not; this becomes an important distinction. Retail stores will included wholesalers and distributors. They're just at a different level, but they are still basically a pass through for inventory.

All of these businesses are going to have fixed assets, but at the retail level the inventory is valued January 1, as is all other property, but it's based on the prior year average of what they had for sale. And it's based on what the owner paid for it. We don't care what the retail value of inventory is going to be, we are not in the income tax basis, we're valuing their inventory at what they paid for that.

Then the fixed assets, that's the property used to do something, it's not held for sale, it's held to be used. It's going to consist of furniture, fixtures machinery and equipment, and depending on the type of the business there'll be varying amounts of these four types.

Then we move into manufacturers. They're still businesses, it's commercial property, but on kind of a larger scale. Their inventory is a little more complicated. They're going to have raw materials that, through a work process, is converted to finish goods. All three of these types of inventory will exist at any given time. We were talking about using that prior your average, but in any instant in time last year, they had material waiting to be processed, they had materials being processed, and they had finished goods sitting down in the warehouse. So all three of these tabs are distinctly different forms of inventory.

Then there are supplies. Pretty much all businesses will use supplies of some type, but manufacturers much more than others. There is a provision under Arkansas law, that some part, sometimes 99%, but some part of a manufacturer's inventory is considered to not have status. That is no taxable location in the state. If the goods they produce are destined for sale outside of Arkansas, then we take a percentage of those sales compared to their total, and apply that same percentage to each of the three types of inventory, and that is not taxed. Again, it has no status.

This is a provision that the manufacturer needs to ask the assessor to let them apply for. The assessor will review the information provided and make a determination as to whether this is going to be received. It's a good boost for the manufacturers and the state. And again, all inventories are based on the prior year average of what they had.

And the manufacturers fixed assets...I mentioned earlier, a service business is going to run a little heavier towards furniture and fixtures. They don't have any active process. A retailer will have a better mix. Say a supermarket: they're going to have quite a bit of furniture and fixtures in terms of shelving encounters and things of that sort. But they're also going to start having more machinery and equipment. The dairy case and the coolers and freezers and such.

Manufacturers are going to run very heavily towards machinery and equipment. They're there to make something. They're going to have some furniture and fixtures. They have a break room, they have offices and things of that sort. I may have a lot of shoving in a warehouse or something. But most of their property tend to be in the form of machinery and equipment. They may have a lot of shelving in a warehouse or something, but most of their property tends to be in the form of machinery and equipment.

That machinery and equipment we can break down into general and specialized, and that will become important when we started looking at depreciation. General machinery and equipment, you're going to find in almost any plant. Pumps, motors, conveyors material and equipment, things of that sort.

But the specialized equipment will be tied to what that plant makes. Whether it's a bottling plant or a saw mill or steel mill or paper mill—in many cases in Arkansas—they have very specialized, and usually that means very expensive, equipment.

Now personal property is valued using the same three approaches as all others: the cost approach, the sales comparison approach and the income approach.

Automobiles and vehicles, most of the individual personal property, we obtain data from a supplier in the marketplace and provided to the assessors. So this property is more or less valued using the sales comparison. That is, we obtained market data for the basis of value, and that's about as far as it goes for personal property.

All other personal property, all that machinery and equipment in those plants and things of that sort, are valued using the cost approach. By law, the owner is to report a list of all their property, what they paid for it—that is the cost—and the date of their acquisition. We need to know how old it is to calculate depreciation.

The income approach says the value of property is based on its future potential to produce income. That works pretty [well] for a single property, but it's not really good in the mass appraisal of personal property in the way that we do it. If I needed to value, say, a coffee machine, I can go out and see what similar machines rent for on longer term lease. I can take that income stream and get an opinion of value based on that.

But it doesn't work. If you look at the office, you're in right now, and all the different kinds of personal property, there's no way you could get income streams for all this stuff and apply this method. Forget doing it for everything in the county. This is not a really good workable method for that.

So we'll talk mostly about the cost approach here. The cost basis that we're going to use is, as I said, what the owner paid for it. It should include installation costs, whatever it takes to bring that asset to a point of productivity. We call that a highest, best use. The owner is, by law, supposed to report that to the assessor.

Now 26-26-910, one of my personal favorite statutes, says the assessor will determine whether that cost appears to be correct or not. And if they feel like it's not, the assessor has the authority to use some alternative. We actually provide what we call square foot rates to the assessors they can use in this instance. We've done research on the typical cost per square foot for the inventory or the fixed assets of about 80 different types of businesses. That only leaves several hundred that we don't have, but where we do have it, we've tried to make this information available for assessors. We don't recommend it as a primary evaluation method, but it certainly would give them a good opinion value if the owner is not providing adequate information or maybe doesn't assess at all—that happens too.

Depreciation is the next phase, if you will, of the cost approach. We start with the cost, we consider the age and condition of the asset, so we take away its loss in value, where it has been used, and the result is the market value. If we can use the sales comparison approach, when a knowledgeable buyer and seller come to agreement as to the value of an item, they've taken things like depreciation into account. So it's kind of automatic there.

In the cost approach, we have to apply it as a phase or a step in the process. The schedules that the assessors use we provide to them. They tie an economic life to the type of property. For example, service businesses, offices and such, overall we feel like the assets in those businesses have about a 10-year life down to a minimum value. We used 12 (years) on retail businesses and depending on the industrial type, they may go from 12 up to as much as 20 on really durable things like feed mills and things of that sort.

Depreciation takes three basic forms. There's physical deterioration, that's the one everybody's familiar with, whether you know it or not. It's ordinary wear and tear, it results from use and pretty much everything short of an anvil is going to suffer that. It's measured using the schedules I mentioned that we provide to the assessors.

The next form is functional obsolescence. It's a little more esoteric. Functional obsolescence means there's nothing wrong with the property, but it has lost value in in the market, most often because of technological innovation in the case of personal property.

Computers are probably the best example or anything digital or anything electronic. They come out with a new iPhone every six months. Computers have gone through an evolution, where they don't change quite as quickly as they used to. But still, they're going to lose value quicker than a desk or a set filing cabinets or something. This is functional obsolescence. It is inherent in the property, and again, there's no loss in productivity it's just a loss in value.

Now, all computers are going to suffer obsolescence, all electronic goods, things of that sort. So we have built that into their schedules that are provided to the assessors they don't need to worry about measuring separately.

Then the most esoteric, the rarest of the types of depreciation is economic obsolescence. In the world of what we call fee appraisal, appraisals for banks and such, it's often called external obsolescence. And it's because it results from forces outside of the property itself. These usually result from changing consumer demand or government regulation. There's still nothing wrong with the property, it's just not worth anything because you can't use it.

I grew up in a house that had asbestos shingles--some y'all may be old enough to recall that. The government decided a long time ago that asbestos causes cancer. If I had a machine that all it did was make asbestos shingles, it would be worthless now. It's only value would be as scrap metal, but if that could be adapted to some other use, if it could be converted to make slate shingles or something, then that obsolescence would not occur. This is a little unusual and pretty tough to measure, but it's out there. And I should point out, it affects that specialized equipment I was talking about. It's not going to affect pumps and motors and things of that sort, there's always a secondary market for those.

[Wayne] Thank you very much, Steve, for your presentation. I certainly learned a lot, especially on business personal property valuation...

[Steve] Well, thank you.

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[Wayne]…which I hadn't seen before. The first question we have is: I paid taxes on my vehicle when I bought it, so why do I have to pay taxes on it every year?

[Steve] You know, that's a great question and one that we get pretty often. When you purchase a car or new clothes or any, almost any consumer goods, I think, except drugs and maybe food, you pay a tax. It's a sales tax, it's a tax on consumption. It's levied by the state and a small portion, maybe by the local governments. That tax issues to operate state government, it helps fund the schools and provides even turnback funds to local governments.

But, it's a tax on consumption levied by the State. It has really nothing to do with the property tax. The property tax is leveled only by local governments: schools, cities and counties. As Wayne mentioned earlier, it stays entirely within your county. That makes it the most beneficial tax, in my humble opinion, as far as for where you live. It's used, not just for the schools, there's often a dedicated millage for roads or for libraries, police and fire pensions, things of that sort.

And it is based on the value of the property: we call it ad valorem. As the property ages the tax will go down because the value has decreased. It floats with the value. The only time really you'll see a property tax go up on an item, I guess, would be if you had a millage change in your school district.

[Wayne] Thank you, Steve. Second question, we have: Can I challenge a personal property assessment on my vehicle? I had an accident with my vehicle and it was not restored to original condition and so therefore the market value of my vehicle, I don't think it is the assessed value again.

[Steve] The first thing to do is talk to the assessor. The assessor is the authority in a county and has the ultimate say in the value of your property initially. If you believe that the condition, the high mileage or the physical condition of vehicle or something warrants a lower value, you need to go talk to the assessor about it.

They may want to review it. I used to work for an assessor that she would listen to some folks, she you would consider, but she also took pictures, she checked the odometer, things of that sort. And but it's up to the assessor whether an adjustment is going to be an order.

If the assessor doesn't provide you with what you consider adequate relief. You have the right to go to your local Board of Equalization. Make an appointment to go visit with them, you need to take them evidence as to why the value is not what the county says its worth.

[Wayne] Okay, so we have one final question that's been raised. Are government entities and churches required to pay the personal property tax on their vehicles, fixtures and equipment?

[Steve] In a nutshell, no, almost all government property belongs to the public. It belongs to you and me, is there for the purpose of public use and is not taxed period.

As long as property is used for worship, at least partially maybe primarily for worship, it's considered to be exempt from taxation. Now, the example we used to always use is, the church as a couple acres of land next to the church for a parking lot. That's fine as part of the church.

They get 40 acres next door that they lose that grow soybeans on, that's not going to be exempt. If the property, just because it belongs to a church, if it's used for something other than worship purposes, particularly producing income, then it becomes taxable just like any other similar properties.

[Wayne] Thank you, Steve. We appreciate your presentation today. I'd like to draw your attention to our next webinar, next Friday, July 27 which will be on utility and carrier assessments and the presenter will be a Sarah Bradshaw, who is the Director of the Tax Division of the Arkansas Public Service Commission.

And before we go, I would like to also remind you that there are a number of other resource available on property assessments and the property tax.

[GUITAR MUSIC PLAYS]