

# Equality and Uniformity in Texas: A First-Time Remedy for an Old-Time Right

James Popp and Allan Carmichael

Even though for 154 years the Texas Constitution has guaranteed equal and uniform treatment in taxation, only recently have taxpayers had recourse to a potential remedy. This article reviews the new equal and uniform standard in Texas and how it will affect appraisals in that state.

**THE FIRST TEXAS** Constitution of 1845 provided for equality and uniformity of taxation, as have the numerous constitutions adopted since then. Similarly, the constitutions of most other states also contain a similar concept. The Texas Constitution in Article VIII, Section 1, currently provides that "taxation shall be equal and uniform." Thus, for 154 years, the Texas Constitution has boldly proclaimed equal and uniform treatment in taxation. Despite the bold proclamation of this old-time principle, however, its application and usefulness as a remedy has been so limited as to be virtually nonexistent. This hopefully will change as a result of the new equal and uniform remedy adopted by the Texas Legislature in 1997. The new equal and uniform remedy provides taxpayer relief based on a comparison of the subject's tax value to the tax value of comparable properties, as opposed to the traditional sales ratio approach.

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**JAMES POPP** is a partner in the law firm of Popp & Ikard, in Austin, TX. Popp & Ikard devotes its practice to the representation of taxpayers and is the Texas member of the American Property Tax Counsel.  
**ALLAN CARMICHAEL** is a MAI and in-house appraiser for Popp & Ikard.

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**A BRIEF HISTORY OF EQUALITY AND UNIFORMITY IN TEXAS**

The hope for a meaningful remedy for purposes of equality and uniformity appeared in a 1943 Court of Appeals case styled *Dallas National Bank v. Dallas County*.<sup>1</sup> The taxpayer protested and argued that its land was overvalued in comparison to adjoining tracts. The assessed values were as follows:

Tract	Acreage	Assessed Value Per Acre
Subject	153	175
Lindsey`	305	35
Aronson	35	20
Armstrong	99	20
Luna	68	29
Schreiber	116	28
Schreiber	70	28
Daniel	102	24

Despite evidence showing that the tracts and the subject were of the same approximate kind and value, the trial court held that: (1) the valuation standing alone could not be considered arbitrary or excessive if the appraisal was admittedly less than the fair market value of the property; (2) there was no support for a charge of fraudulent assessment in the sense that the assessment was intentionally made with a view of casting an undue proportion of taxes upon the subject; and (3) there was no violation of equality and uniformity because the valuation of adjoining lands, disproportionate as they were, was due solely to the mistaken but honest judgment of the assessor.

On appeal, however, the court held that: (1) taxes levied on the subject on a basis of 70 percent of its full value in contrast to 10 percent on adjacent land resulted in inequality; (2) the subject's assessment was unconstitutional, though based on less than actual value, when it was assessed on a greater proportion of its full value than was used at the same time in the assessment of like and adjacent lands; (3) this was so even though there was no allegation of a system or scheme of unequal taxation on the part of the tax authorities; and (4) the tax authorities upon protest should have proceeded to an equalization of these values either by raising adjoining valuations after notice or appropriately reducing the subject's valuation.

For the next 50 years, this case provided a hope and a basis for a potentially effective taxpayer remedy for violations of the equal and uniform standard. The reality of this remedy, however, never reached the optimistic potential of *Dallas National Bank* and instead the results have generally been decided along two different and distinct approaches. Some courts have denied claims for violations of the equal and uniform standard with regard to

<sup>1</sup> 173 S.W. 2d 558 (Tex. Civ. App. Dallas), *rev'd on other grounds*, 179 S.W.2d 288 (Tex. 1943).

individual properties when they could find evidence of a difference of opinion or judgment on the part of the tax authorities with regard to the treatment of the property. In contrast, other courts have generally only found violations of the equal and uniform standard in connection with a deliberate plan or scheme on the part of the tax authorities. Thus, even though a violation of this standard may be apparent on its face, Texas courts generally find violations only in instances of a deliberate plan.

Texas courts have found no violation of the equal and uniform standard under the following justifications or rationales:

- Equalization boards may act upon their own judgment of what is equal taxation.
- Absolute equality and uniformity in taxation is not required by the constitutional provision that taxation shall be equal and uniform.
- Exact uniformity and equality of taxation is an unattainable ideal, but the board of equalization is charged with the ultimate responsibility of working toward such an ideal.
- Uniformity is satisfied if value of the property of the same class is ascertained by reference to the same standard.
- Mere omissions or errors of judgment by taxing officials in the exercise of honest judgment will not invalidate assessment under the constitutional requirement that taxation shall be equal and uniform.
- A reasonable discrepancy between true value of property and value which it is assessed for taxes will be permitted to cover the difference in judgment regarding value of property.
- While use of 40 percent of market value for one property and 32 percent for a bulk of properties might well be unlawful discrimination, since it would be willful, the same assessments would not necessarily constitute discrimination if it was the result of an honest difference of opinion as to value.

Other Texas courts have found a violation of the equal and uniform standard based on the following justifications or rationales:

- Where the property of individuals was assessed at 50 percent of its real value in accordance with a deliberately adopted plan, an assessment of property of a railroad at full value violated equality and uniformity of taxation.
- Assessing all land in school districts at an arbitrary value of \$20 per acre was held in violation of the constitutional provision of equality and uniformity.
- Tax plan sought to be implemented by county was fundamentally erroneous as placing oil and gas properties at 100 percent of market value while all other property was assessed at varying percentages having no basis in market value.
- Valuation of all property in particular zone at some value per acre without regard to character of land and nature of improvements is in error.

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- Where board did not value mineral properties according to market value as required by law, but adopted a fundamentally different and wrong principle, such valuation was void.

The protection afforded by the equal and uniform standard, however, was minimal because a deliberate plan was difficult to prove. Recognizing this, the first attempt at an effective statutory remedy for unequal appraisal was adopted by the Texas Legislature in 1977 under Article 7345f.<sup>2</sup> That statute allowed the first direct appeal and correction of a value by stating:

In fixing the value of the property in question, the court or jury shall determine the cash market value and multiply that by the assessment ratio, if any, in effect for the taxing authority involved.

Thus, the equal and uniform remedy became dependant upon proof of the applicable assessment ratio. In a significant case expanding and explaining this remedy, a taxpayer in *City of Dallas v. Union Tower Corporation*<sup>3</sup> brought suit against the tax authorities under Article 7345f and Article VIII, Section 1, claiming that its property was appraised unequally in comparison to other property in the county.

The subject property was a downtown office building with a stipulated market value of \$41,500,000 as of January 1, 1981. The property was appraised by the tax authorities at a value of \$37,738,396. The taxpayer contended that the property should be appraised at \$26,560,000 based on the allegations that it was appraised at a higher percentage of its value than other properties appraised by the tax authorities.

The taxpayer relied on several expert witnesses. The experts obtained records of 1,196 real estate sales within the taxing authorities' boundaries for the period between June and December of 1980. Based upon these records, the experts determined the tax valuations to be 61 percent of the sales prices by calculating the ratio of the amounts for which the properties were appraised by the tax authorities for 1981 to their sales prices. An expert also testified that this procedure was consistent with the practices recognized as valid within the science of statistics and the conclusions reached were accurate within 2 percent to 3 percent. The taxpayer also called as an expert the executive director of the State Property Tax Board who testified that the tax authorities appraised residential property at 60 percent of its market value. This testimony supported the previous sales testimony. As a result, the experts testified that if the taxpayer's property had been appraised with respect to its stipulated market value of \$41,500,000, it should have been appraised at \$26,560,000 based upon the equal and uniform standard.

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<sup>2</sup> Tex. Rev. Civ. Stat. Ann., art. 7345f (repealed).

<sup>3</sup> 703 S.W.2d 275 (Tex. Civ. App. Dallas 1985, writ ref. n.r.e.).

The tax authorities argued that the evidence showing they appraised property at less than market value did not mean that they used a "ratio of assessment" in their plan for appraisal as that term was used in Article 7345f. In fact, they argued that the taxing authority's governing body had passed resolutions directing that the property be appraised at 100 percent of its market value. The tax authorities also argued that their goal under mass appraisal was a target appraisal of 85 percent of market value.

Contrary to previous cases, the Dallas Court of Appeals held that Article VIII, Section 1 makes unequal appraisal illegal without reference to whether it was done pursuant to an adopted plan. The taxpayer's proof that tax authorities appraised the subject property at 90 percent of market value and other properties at an average of 64 percent of their values, whether by proof of "level of appraisal" or a "ratio of assessment," established the illegality of the appraisal. Furthermore, even though the property was appraised at less than market value, the evidence that other property was appraised at an actual ratio substantially lower than the ratio applied to the subject established discrimination which entitled the taxpayer to relief under the constitutional requirement that taxes be equal and uniform.

### THE NEW TAX CODE REMEDY FOR UNEQUAL APPRAISAL: A START

In 1979, the Texas Legislature adopted the Property Tax Code, which provided an entirely new system of appraisal and taxpayer remedies. For the first time, a specific remedy for unequal appraisal was provided by a statute which in effect was quite similar to that approved by the court in *Union Tower*.<sup>4</sup>

<sup>4</sup> The statute has undergone several minor changes since adoption:

**1 Sec. 42.26. Remedy for Unequal Appraisal**

The district court may not grant relief on the ground that a property is appraised unequally in comparison to the level of appraisals of other property in the county or in the appraisal district unless the appraised value of the property varies at least 10 percent from its value calculated on the basis of the aggregate mean level of appraisals in the county or district, as applicable. In that event, the court shall order the appraised value changed to the value as calculated on the basis of the aggregate mean level of appraisals in the county or district, as applicable. (1979)

**Sec. 42.26. Remedy for Unequal Appraisal**

The district court may not grant relief on the ground that a property is appraised unequally in comparison to the level of appraisals of other property in the appraisal district unless the appraised value of the property varies at least 10 percent from its value calculated on the basis of the weighted average level of appraisals in the district. In that event, the court shall order the appraised value changed to the value as calculated on the basis of the weighted average level of appraisals in the district.

**Amended by Acts 1981, 67th Leg., 1st C.S., p. 174, ch. 13 § 153, eff. Jan 1, 1982.**

**Sec. 42.26. Remedy for Unequal Appraisal.**

- (a) The district court shall grant relief on the ground that a property is appraised unequally if the appraisal ratio of the property exceeds by at least 10 percent the median level of appraisal of:
- (1) a reasonable and representative sample of other properties in the appraisal district; or
  - (2) 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.

**Amended by 1981 Tex. Laws (1st C.S.), p. 174, ch. 13, § 153; amended by 1983 Tex. Laws, p. 4924, ch. 877, § 3; amended by 1985 Tex. Laws, p. 6149, ch. 823, § 3; amended by HB 432, 71st Leg., eff. June 15, 1989.**

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Once again, however, the optimism regarding the new statute did not live up to the reality of its usefulness. The usefulness of the statute was affected by two things. First, with the adoption of this statute, the Legislature also passed Section 42.09 of the Tax Code, which states that the procedures prescribed by this title for adjudication of the grounds of protest authorized by this title are exclusive. The language forms the basis for the argument that a taxpayer could only use the statutory remedy and that the common law approach under *Dallas National Bank* was no longer available to a property owner. Second, the remedy set forth in the statute was very expensive to utilize because it required a sales ratio study. The statute required a property owner to take the following steps:

1. Determine a reasonable number of other properties similarly situated to, or of the same general kind of character as the subject property;
2. Determine an appropriate sample of these properties;
3. Determine the market value of each property in the sample;
4. Determine the ratio of the appraised value to the market value of each property in the sample;
5. Determine the median ratio of the sample;
6. Determine the market value of the subject property; and
7. Apply the median ratio of the sample to the market value of the subject.

Because of the inherent economic limitation of requiring an appraisal of all properties in the study including the subject, this remedy was rarely used.

### **THE NEW EQUAL AND UNIFORM STATUTE: A FIRST-TIME REMEDY**

In 1997, the Texas Legislature added Section 42.26(d) to the Texas Property Tax Code effective for the 1998 tax year. The statute provides:

The District Court *shall* grant relief on the ground that a property is appraised unequally if the appraised value of the property exceeds the median appraised value of a reasonable number of comparable properties appropriately adjusted.

This language was added to the district court appeal procedures of the Property Tax Code. The suggested approach and considerations in this new equal and uniform remedy are set forth below.

#### **Equal and Uniform at the Appraisal Review Board**

At the same time that the Legislature was adding the equal and uniform remedy to the district court appeal procedures, it also amended the existing equal and uniform remedy to

the administrative protest procedures.<sup>5</sup> The Legislature did not include the same language in the administrative statute.

This difference in language raises two issues at the administrative protest level. First, there is some question as to whether the new remedy is available at the administrative level. Second, there is an issue as to whether some evidence relating to equality and uniformity must be presented at the administrative level in order to raise the issue at district court.

With regard to the first issue, the term "median level of appraisal" as used in Section 41.43 of the Tax Code is defined to mean a comparison of appraised value to market value, as was previously discussed with regard to ratio studies. This phrase is different from the new language referring to "median appraised value." Thus, appraisal districts have argued that the new remedy allowing the comparison of appraisal values to the subject is not available at the administrative level. They argue that the new amendment only broadens the sample types available for a sales ratio study.

Second, even if the new district court remedy is not available in an administrative protest, it is prudent for a taxpayer to raise equality and uniformity concerns at the protest hearing. Although there is no case law explicitly on point, appraisal districts have contended that if a taxpayer does not raise an issue at the administrative protest hearing, the taxpayer cannot raise the issue for the first time in an appeal to the district court. This argument is based on the concept of exhaustion of administrative remedies. Taxpayers would, of course, argue that the issue need not be raised at the protest hearing because the Legislature gave the courts primary jurisdiction regarding the issue and the statute indicates that the administrative process is intended to be informal in nature. A cautious approach would dictate raising the issue at the protest hearing until this issue is decided by the courts.

### **Selection of Expert Witnesses**

It will be necessary at trial to have a witness testify as to the new equal and uniform analysis. There are no experts with experience and credentials in the determination of equal and uniform studies, as there are in determinations of market value. The expert will be required to determine elements of comparability, select sufficient comparable properties, and make adjustments. The expert must be familiar with real estate markets and value concepts. These principles are all familiar tasks for an appraiser and would form the experience necessary to be qualified to perform an equal and uniform study. Thus, it is suggested that a

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<sup>5</sup> Item (3) was amended to Subsection (b) of Section 41.43, Tax Code:

- (b) A protest on the ground of unequal appraisal of property shall be determined in favor of the protesting party unless the appraisal district establishes that the appraisal ratio of the property is not greater than the median level of appraisal of:
- (1) a reasonable and representative sample of other properties in the appraisal district;
  - (2) 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 of the protest; or
  - (3) a reasonable number of comparable properties appropriately adjusted.

taxpayer retain a member of the Appraisal Institute and perform the study under the auspices of the Uniform Standards of Professional Appraisal Practice.

### **Selection of Comparable Properties**

The statute requires the appraiser to select "comparable" properties. The statute does not, however, define the word "comparable." A reasonable approach would be to define the universe of comparable properties in a process similar to that undertaken by an appraiser for purposes of a sales comparison approach or a comparable rent approach.

An appraiser should consider the following selection criteria:

- *Use.* The comparable should be selected based on similar use such as apartment, office building, or vacant land.
- *Competitive Set.* The comparables should be selected based upon whether they are competitive in the market place with the subject. This is often expressed in terms of class of property.
- *Neighborhood.* The comparables should generally be located within the same geographic location, whether it is a neighborhood or business district.
- *Size.* The comparables should generally be selected based on similar size to the subject.

### **Reasonable Number of Comparables**

The statute next requires the appraiser to select a "reasonable number" of properties for comparison. The statute provides no guidance as to what constitutes a reasonable number. The predecessor statute mentions a reasonable and representative sample. It is clear that the new statute does not envision this same sort of statistical test. It would appear that whatever the number of comparable properties that would be sufficient for purposes of forming an opinion under the sales comparison approach or for determining rent from rent comparables would be a starting point for sufficient number for this analysis. Consideration should also be given to the number and quality of the comparable properties. The appropriate number of comparables based upon this analysis should be left to the discretion of the appraisers.

### **Appropriate Adjustments**

The statute next directs that the comparable properties are to be "appropriately adjusted." The statute once again provides no guidance. A reasonable approach is outlined by *The Appraisal of Real Estate*, which sets forth appropriate elements of comparison for both a sales comparison approach and a rental comparison as follows.<sup>6</sup>

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<sup>6</sup> The Appraisal Institute, *The Appraisal of Real Estate*, 404, 481 (11th ed. 1996).



### Elements of Comparison

<i>Sales Approach</i>	<i>Rental Analysis</i>
Property Rights Conveyed	Property Rights Conveyed
Financing Terms	_____
Conditions of Sale	Conditions of Rental
Expenditures Made	_____
Immediately After Purchase	
Market Conditions	Market Conditions
Location	Location
Physical Characteristics	Physical Characteristics
Economic Characteristics	Economic Characteristics
Use	Use
Nonrealty components of value	Nonrealty components of value

Of these characteristics, the most appropriate elements directly attributable to the value of a property are location, physical characteristics, economic characteristics, and use. Use was a selection criteria. Thus, the remaining three were utilized for adjustments.

*The Appraisal of Real Estate* provides an excellent discussion of the adjustment process.<sup>7</sup> In general, the adjustment process starts with a unit value. For most commercial property, the appraised value per square foot is an appropriate measure. The comparable properties are reviewed and compared to the subject based on location, physical characteristics, and economic characteristics. The comparables are then adjusted for each characteristic to make them equal to or similar to the subject. The appraiser then adjusts the tax appraised value for each comparable based upon the individual characteristics.

#### **Final Opinion Based on Median Adjusted Appraised Value**

The adjusted appraised values per square foot are then arrayed. The median adjusted appraised value is selected and applied to the square footage of the subject to derive the equal and uniform appraised value for the subject.

#### **AN EQUAL AND UNIFORM EXAMPLE**

The subject property was a 290,000 square foot, Class-A office building in 1986. It had been purchased during the prior tax year for \$40,600,000 (\$140 per square foot) and the appraisal district had valued it for tax purposes based upon the sales price. Thus, after a determination that the sales price was market value for fee simple property tax purposes, the

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<sup>7</sup> *Id.* at 418.

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only remedy available to the taxpayer was whether the sales price was equal and uniform in comparison to the appraised value of comparable properties.

The appraiser reviewed the appraisal records and based upon use, competitive set, neighborhood, and size selected five office buildings considered comparable to the subject. The subject and five comparables are summarized in the following table.

**Table 1.**

<b>Property</b>	<b>Subject</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
Location	Loop	Lake	Loop 360	Loop 360	Loop 360	Loop 360
Appraised	\$140.00	\$145.02	\$140.31	\$135.26	\$117.35	\$110.61
Size (SF)	290,000	102,186	125,360	158,636	276,950	350,000
Year of Construction	1986	1984	1986	1987	1983	1985
Land-to-Bldg.	2.47	3.30	2.60	3.96	2.50	2.30
Occupancy	97%	100%	97%	97%	95%	97%
PGI/SF	\$18.00	\$20.00	\$21.00	\$21.00	\$18.00	\$18.50
Expenses/SF	\$ 7.00	\$ 6.70	\$ 7.00	\$ 7.00	\$ 7.00	\$ 6.70
NOI/SF	\$10.46	\$12.70	\$13.37	\$13.37	\$10.46	\$11.25
Comments	Average quality building, convenient location	Lake views average quality building	Average quality building located near high-tech center	Average quality building located near high-tech center	Located near subject, average quality similar in physical characteristics, age, and income potential	Located just south of subject in a suburban location similar in physical characteristics age, and income potential

**OVERALL OBSERVATIONS:**

Subject property is appraised at or near properties in superior and/or lake views.  
 Subject comparable in physical characteristics and net operating income (NOI) of property appraised at \$117.35 per square feet.  
 Appraised value is in line with properties with greater land area.  
 Subject appraised value is in line with higher potential gross income.

**ELEMENTS OF COMPARISON TO CONSIDER:**

Location, physical characteristics, achievable rents, tenant mix, condition of property, nonrealty components, etc.

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Prior to consideration of variances from the subject, the comparables form a value range of \$110.61 to \$145.02 per square foot of gross building area. As indicated, the variances of the comparables from the subject were considered and adjusted in order to determine an equitable appraised value. The variances adjusted for in this instance consist of location, physical variances, and income potential.

### Location

Location plays a vital role in the ability of a project to be successful. Comparable 1 is located along Loop 360 and benefits from lake views enabling the property to capture greater rents. Examples 2 and 3 are located within an area known as the Golden Triangle, which has been developed to compliment the booming high-tech industry. Therefore, comparables 2 and 3 have received a negative 10-percent adjustment for their superior location. Comparable 5 is located approximately one mile south of the subject in an area consisting of limited development and received a positive 2-percent adjustment to compensate for inferior location. Comparable 4 is similar in location to the subject.

### Physical Characteristics

An adjustment for physical differences is generally recognized in the market. The subject contains a total of 290,000 square feet of gross building area and is of average quality. Comparables 1, 2, and 3 are considerably smaller than the subject and are deemed superior. Therefore, their overall value was adjusted downward by 5 percent. Comparable 4 is approximately the same size and quality as the subject and does not require an adjustment, while Number 5 is deemed inferior and adjusted upward by 5 percent.

### Economic Characteristics

Comparables 1, 2, and 3 benefit from being able to generate higher rents as a result of tenant mix, operating efficiencies, and ability to pass on more operating cost to tenants. In this instance, these three properties have received an adjustment of negative 2 percent.

All of the adjustments made to the comparables are shown in Table 2.

<b>Property</b>	<b>Subject</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
Assessment						
PSF	\$140.00	\$145.02	\$140.31	\$135.26	\$117.35	\$110.61
Physical	-----	-5%	-5%	-5%	-----	+5%
Location	-----	-10%	-10%	-10%	-----	+2%
Economic	-----	-2%	-2%	-2%	-----	-2%
<b>Indicated Value</b>	-----	<b>\$120.37</b>	<b>\$116.45</b>	<b>\$112.27</b>	<b>\$117.35</b>	<b>\$116.14</b>
Median = \$116.45						

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Upon conclusion of the adjustments, the applicable value range is determined to be \$112.27 to \$120.37 per square foot. The original range was \$110.61 to \$145.02.

**Median Appraised Value Table**

The comparable properties are then arrayed from highest per square value to the lowest.

<b>Property</b>	<b>Adjusted Appraised Value</b>
Comparable 1	\$120.37 PSF
Comparable 4	\$117.35 PSF
Comparable 2	\$116.45 PSF
Comparable 5	\$116.14 PSF
Comparable 3	\$112.27 PSF
Median	\$116.45 PSF
Subject Appraised Value	\$140.00 PSF or \$40,600,000
Subject Appraised Value at Median	\$116.45 PSF or \$33,770,500

The median adjusted value is \$116.45 per square foot. This is applied to the 290,000 square feet of the subject building to arrive at an equal and uniform value of \$33,770,500.

**CONCLUSION**

For the first time in Texas, an equality and uniformity remedy is available to taxpayers. The example property had a sales price and a taxable value of \$40,600,000. Previously, there would have been no tax relief. Now, an equal and uniform comparison to comparable properties results in a tax value of 33,770,550, a value reduction of \$6,829,450 and a tax savings of \$177,500. This first-time remedy will prove to be an effective tool for taxpayers.