

**CITY OF MADISON
OFFICE OF THE CITY ATTORNEY
Room 401, CCB
266-4511**

Date: September 29, 2006

OPINION #06-003

TO: Mayor Dave Cieslewicz
FROM: Michael P. May, City Attorney
RE: Valuation of Inclusionary Zoning Housing Units

You have requested my opinion on how housing units covered by the Inclusionary Zoning Ordinance are to be valued for property tax purposes.

This opinion will examine the relevant provisions of Wisconsin's property tax assessment statutes and the provisions of the Inclusionary Zoning Ordinance that could impact the application of those assessment statutes. I will then set out how those two laws working in tandem could impact the tax assessments of housing units covered by the Inclusionary Zoning (IZ) Ordinance.

As will be explained in more detail below, it is difficult to speculate on the exact impact of the IZ Ordinance until units covered by the law are sold and resold. However, it is likely that IZ units will approximate the value, and therefore the assessments, of comparable non-IZ units. This is because the restrictions on the value of IZ units imposed by the IZ Ordinance are limited in time and therefore have limited impact on the assessment process.

A. Wisconsin's Real Property Tax Assessment Laws.

Sec. 70.32(1), Wis. Stats., mandates the manner in which real property is to be valued: "... the value which could ordinarily be obtained therefore at private sale." A recent sale of the property is considered by the courts to be the best indication of a property's value.¹ However, this section provides instruction as to what constitutes a valid "sale" for assessment purposes. The section reads in pertinent part:

"In determining the value, the assessor shall consider recent arm's-length sales of the property to be assessed if according to professionally acceptable appraisal practices, those sales conformed to recent arm's-length sales of reasonably comparable properties; recent arm's-length sales of reasonably comparable properties; and all factors that, according to professionally acceptable appraisal practices, affect the value of the property to be assessed."

1 *Campbell vs Town of Delavan*, 210 Wis. 2d 240, 565 N.W.2d 209 (Ct App 1997).

An "arm's-length" sale is defined as a transaction on the open market negotiated by an owner willing but not obligated to sell, and a buyer willing but not obligated to buy. In that circumstance, full value or fair market value may be established by the sale.² However, the sale must also meet the section's qualifying condition that it conforms to sales of reasonably comparable properties.³

If the full value of the property is not established by a valid arm's-length sale, the value may be established through sales of reasonably comparable properties. Reasonable comparability is established by analyzing properties' size, location, amenities, finishes, quality of construction and interior materials, existing appraisals, number of bedrooms and bathrooms, age, current physical condition, existence and type of restrictions, if any, and the like.

If there is neither a valid arm's-length sale nor a sufficient number of sales of reasonably comparable properties, assessors are to use the third tier of the statutory assessment model – all factors that affect the value of the property. These would include cost, depreciation, location, book value, insurance carried on the property, value asserted in marketing materials, fair market value appraisals, and replacement value to name a few as examples.

The impact of the IZ ordinance on the assessment also turns on the assessment date, which is the close of January 1 each year⁴, the initial land restriction (sale price based on buyer's income) and the 180-day marketing period.

B. The Restrictions on Value in the IZ Ordinance.

The IZ ordinance is set out in §28.04(26), MGO, and contains the following restriction. The ordinance limits the price of an IZ unit to no more than 30% of the monthly income for the applicable area median income of the buyer. The price of a lot for an IZ unit shall be not more than 25% of the qualifying sales price of an IZ dwelling unit that will be constructed on the lot. Once the IZ unit is sold, there is no longer a restriction on sales price for future re-sales of the unit. In addition, the City has an option to purchase IZ units after the initial qualifying sale. However, because the City's option to purchase is now at 100% of fair market value, the option is not considered a restriction.

2 *State ex rel. Levine v Board of Review of Village of Fox Point*, 191 Wis. 2d 363, 372, 528 N.W.2d 424 (1995)

3 Our research and our discussions with the City's Chief Assessor strongly suggest that a sale of a property restricted by considerations such as those contained in the IZ ordinance would not be considered comparable to sales of fully unrestricted properties

4 Sec. 70.01, Stats

C. Application of the IZ Restrictions to Assessments—The Theory.

If a lot is designated as an IZ lot, and a home is constructed or under construction **and** the January 1 assessment date falls before the 180-day marketing period has begun or within the 180-day marketing period, **and** the property has not sold to a qualified buyer, the assessed value will be based on the theoretical sales price to a qualified buyer calculated according to §28.04(26)(e), MGO. This is a restricted value due to the land use restriction in place, and the assessment should match the value established by the IZ restrictions.

In the above situation, if the property sells within the 180-day marketing period to a qualified buyer prior to January 1, the initial sale price likely will not be the assessed value for that January 1 assessment date because the land use restriction is lifted upon the sale of the property, and the property is no longer a restricted property. In this case, the assessment will be made at 100% market value based on all available information. Presumably, this amount should be the value of comparable units sold without any IZ restrictions.

If a lot is designated as an IZ lot and a home is constructed or under construction and the January 1 assessment date falls after the 180-day marketing period, the assessed value will be based on the 100% fair market value of that property. This property will never be restricted on the January 1 assessment date because the IZ land use restriction would have expired after the 180 days.

As can be seen by these examples, there is a limited time when the 180-day restriction has any impact on the value of the IZ unit: once the unit is sold, all restrictions expire, and the 180-day restriction will only impact the value if the restriction is in place on the January 1 assessment date.

D. Application of the IZ Restrictions to Assessments -- The Actual Impact

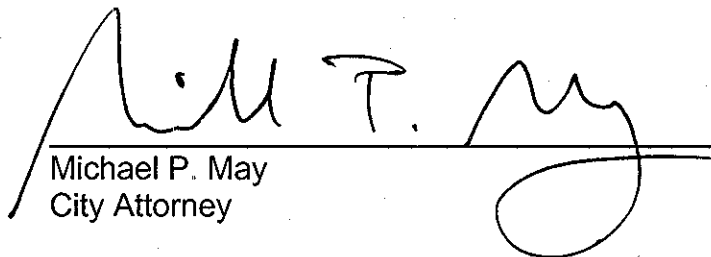
Whether the theoretical impact set out above actually happens in the real world has to await actual sales and re-sales of IZ units. Because of the theoretical variations, the lack of knowledge of whether or not other IZ units or other reasonably comparable properties have sold, or whether fair market value appraisals of the property exist, we cannot now predict at what amount any given IZ unit will be assessed, except for those theoretical values described above. At best, all we can predict is that it is unlikely that the actual initial sale price will establish the assessed value unless there have been sales of reasonably comparable and similarly restricted properties as discussed above.

As time passes and IZ and comparable units sell, the Assessor's staff will have data available to assess the properties in compliance with the statutes and case law. The Assessor may find that the IZ units do have value comparable to non-IZ units as theorized above, or the Assessor may find that such units may, for market reasons we cannot predict, have some different value. Moreover, we cannot predict what those assessed values might be; for example, even if IZ units are assessed at values similar

to non-IZ units, we cannot predict whether that value will be closer to the initial qualifying sale price of the IZ unit or some other figure.

E. Conclusion.

It is difficult to predict the assessed value of IZ units until such units are subject to sales in the market. From a theoretical standpoint, the IZ restrictions are limited in time and effect, and therefore are not likely to significantly impact the assessments of IZ units.



Michael P. May
City Attorney

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Synopsis: Valuation of Inclusionary Zoning Dwelling Units for Property Tax Purposes Discussed.