Michigan Law Review

Volume 36 | Issue 6

1938

TAXATION - REAL PROPERTY ASSESSMENT

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TAXATION — REAL PROPERTY ASSESSMENT — Based upon the cost-depreciation method applicable to adjacent property, the assessment of the Detroit-Windsor tunnel and terminal resulted in taxes equal to forty-one per cent of the gross revenue for the depression years of 1931-1934. The federal district court enjoined the collection of such amount, and assessed the property by the capitalized income method (seven per cent) plus $3,500 for the value of possible future increased earnings. Upon appeal it was *held* that the injunction on the original levy be affirmed since the cost-depreciation method was erroneous and offensive to the Fourteenth Amendment in not taking account of depressions or the fact that property might be used for other purposes; that the business was in fact a public utility and the capitalized income method of assessment gives a fair value; that the court erred in actually assessing the property and enjoining the collection of any greater amounts; and that the taxing authorities be free to assess the property again for the years involved. *City of Detroit v. Detroit & Canada Tunnel Co.*, (C. C. A. 6th, 1937) 92 F. (2d) 833.[1]

[1] The district court case was Parsons v. Detroit & Canada Tunnel Co., (D. C. Mich. 1936) 15 F. Supp. 986. This case and Great Northern Ry. v. Weeks, 297 U. S. 135, 56 S. Ct. 426 (1936), were the basis of an article, Luce, "Assessment of Real Property for Taxation," in 35 MICH. L. REV. 1217 (1937). The classification of the business as a "single purpose" public utility is therein discussed, page 1250.

[2] 297 U. S. 135, 56 S. Ct. 426 (1936), noted in 35 MICH. L. REV. 174 (1936); 49 HARV. L. REV. 1012 (1936); 24 GEO. L. J. 1005 (1936); 30 ILL. L. REV. 1070 (1936); 84 UNIV. PA. L. REV. 784 (1936).

Since the decision of *Great Northern Ry. v. Weeks*,[2] there have been four federal court cases in which relief from an allegedly too high assessment was sought without proof of discrimination. In *Lehigh Valley Ry. v. Martin*[3] an injunction was refused when the railroad contended that the valuation was excessive as shown by a computation of value by the capitalized income and stock and bond methods, because the railroad did not prove that its method of valuation gave "true value." In *Western Union Telegraph Co. v. Wilcox*,[4] it was held that no injunction should issue because the telegraph company had not proved discrimination, fraud, or a fundamentally erroneous method. In *In re Lang Body Co.*[5] the court refused to confirm a referee's reduction of a tax claim in a bankruptcy proceeding, since the trustee did not offer sufficient evidence to rebut the strong presumption of the validity of a tax assessment. In these cases, as in the fourth, the principal case, the legislative tax policy of uniform distribution of the cost of government was ignored by the court.[6] The modification in the principal case does not necessarily result in greater uniformity. The theory is that the cost depreciation method of assessment was fundamentally wrong because it resulted in a valuation which to the court seemed unreasonably high, and that therefore if any taxes are collected on this assessment or by this method of valuation alone, the city can only collect the amount the court ascertained to be reasonable. Query: Is any method non-arbitrary which places the value higher than that reasonably obtainable by the capitalized income method of assessment?[7] There is a suggestion that a different percentage of capitalization, and also a different sum for the present value of future increased earnings,

[3] (D. C. N. J. 1936) 19 F. Supp. 63. The assessor's value was obtained by aggregating the value of (1) the land on basis of value of contiguous land, (2) the structures by a cost less depreciation computation, (3) the personal property as shown by physical condition, and (4) the franchises based on mere judgments. Great Northern Ry. v. Weeks is distinguished on the fact that there judicial notice of the depression gave the court knowledge that the use of a 1932 assessment in 1933 was arbitrary.

[4] (C. C. A. 8th, 1936) 85 F. (2d) 352. The valuation was determined by averaging the valuations obtained by the cost less depreciation plus going value, the capitalized income, and the sale of securities methods. Great Northern Ry. v. Weeks was distinguished as in Lehigh Valley Ry. v. Martin. In capitalizing earnings the use of six per cent instead of seven or eight per cent was held not to be fundamentally erroneous. "The elaborate and painstaking analysis of the whole testimony . . . leaves no doubt that some computations and estimates of value given by Mr. Murphy involved inaccuracies, but we find no mistakes which reflect any intention or purpose of the commission to depart from or disregard methods which are recognized to be sound and applicable."

[5] (C. C. A. 6th, 1937) 92 F. (2d) 338. Uniform depression reductions for all property in the city was not arbitrary. The opinion was written by the same judge as that of the principal case.

[6] Union Refrigerator Transit Co. v. Kentucky, 199 U. S. 194, 26 S. Ct. 36 (1905).

[7] This is based upon the words of the court. "There is no evidence that the taxing authorities were guilty of any actual fraud but we think that, in persistently adhering to cost less depreciation as a formula for arriving at true cash value and in ignoring the capitalized income method adopted by both the master and the court, they proceeded upon a fundamentally wrong basis." 92 F. (2d) at 837. The factual

than those approved by the district court might be used. No method of ascertaining these two figures is given and in the assessment promulgated by the court as an approved assessment, their determination is as arbitrary as was the original method of assessment herein held invalid.[8] The court mentions that the land and buildings, apart from the tunnel, and valued purely as real estate, might have an actual cash value higher than the capitalized earning value of the entire property.[9] Certainly an assumption cannot be made that when an unprofitable business is put upon an otherwise valuable piece of property, the value of the property is automatically reduced to the capitalization of the income; but if the buildings and land are assessed by the scientific system used in assessing the adjacent property, and only the tube and the underground passages are assessed by the capitalized income method (which really is the only part having value, in any real sense, entirely dependent upon the net income of the entire unit[10]), how should the amount of the income to be allotted to the tube and passages be non-arbitrarily computed?[11] It is submitted that the court rightly modified the district court's decision so that the tax assessors and not the court evaluated the property;[12] but the court should have given some attention to the existence of discrimination and uniformity, since in the principal case the board did not use a method patently arbitrary as was used in *Great Northern Ry. v. Weeks*, viz., use of an assessment for the prior year without considering the depression.[13]

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situation may be that of Great Northern Ry. v. Weeks. "As reflected by the Company's books, using the 1931 assessments as a basis, the assessments for 1932, 1933, and 1934 were arrived at by deductions for depreciation of 2 per cent per annum and two horizontal reductions applied to all property in Detroit and Wayne County of 13 per cent for 1931 and 1932 respectively." 92 F. (2d) at 835. The latter was an evident attempt to allow for the depression. But see In Re Lang Body Co., (C. C. A. 6th, 1937) 92 F. (2d) 338.

[8] It is interesting to compare the principal case with the other cases decided since Great Northern Ry. v. Weeks on the necessity for the taxpayer to prove that the method used was erroneous, that the suggested method is a true measure, that this was a public utility, that the percentage was accurate, and that the present value of future increased earnings is $3,500. The other courts were much less favorable to the plaintiff on these matters of proof.

[9] (C. C. A. 6th, 1937) 92 F. (2d) 833 at 838.

[10] This is recognized in the opinion, (C. C. A. 6th, 1937) 92 F. (2d) 833 at 836.

[11] The court mentions that the value of the building might be higher than the capitalized income value of the *entire* property. If this means that then only will the separate value be considered, the standard approaches the arbitrariness of the Weeks case. If such value is greater, it would certainly be arbitrary to *assume* that the tunnel had no value, or was a liability. See Cleveland, &c., Ry. v. Backus, 154 U. S. 439 at 445, 14 S. Ct. 1122 (1893).

[12] An assessment is a finding of facts upon which administrative action may be predicated. Ex parte Williams, 277 U. S. 267, 48 S. Ct. 523 (1928). "Taxation is legislative and not judicial." Lehigh Valley Ry. v. Martin, (D. C. N. J. 1936) 19 F. Supp. 63 at 75.

[13] It is difficult to tell from the opinion of the principal case, 92 F. (2d) at 835, whether the particular tax to be assessed was deducted from the earnings which were capitalized. If one is consistent with the theory of the capitalized income method, that

should be done. If that is not done, the fact that in an income tax computation the particular tax to be computed cannot be deducted from the income is merely evidence that the capitalized income method has a tendency to make the property tax an income tax. See, Luce, "Assessment of Real Property for Taxation," 35 MICH. L. REV. 1217 at 1220 (1937). The difference between an assessment with such a deduction and one without is quite sizeable, the former being the fraction of the latter as determined by dividing the capitalization figure by the sum of the capitalization figure and the tax rate. In the 1932 assessment in the principal case the former would be approximately 67.6 per cent of the latter.