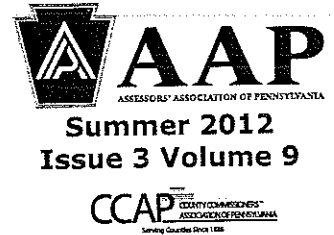


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PA Supreme Court Decision in Tech One: Road Map to Uniformity

By Sharon F. DiPaolo

For years, Pennsylvania assessors and assessment lawyers have been watching and waiting for our Supreme Court's decision in the case of Tech One Associates. The wait is over. On April 25, 2012, the Pennsylvania Supreme Court issued its ruling in Tech One Associates v. Board of Property Assessment Review and Appeals of Allegheny County, 32 WAP 2010 (2012), changing 20 years of practice regarding how leased real property is valued throughout Pennsylvania for purposes of taxation. In short, the Supreme Court ruled that where real estate interests are divided, all interests must be valued to arrive at the whole for purposes of real estate taxation.

To understand why this seemingly common sense ruling became necessary, it is useful to look at the factual background and valuation issues presented by the Tech One case and by the Court's 1992 decision in Marple Springfield, v. Board of Assessment Appeals of Delaware County, 607 A.2d 708 (Pa. 1992).

WHERE WE'VE BEEN: A LOOK BACK AT MARPLE

The Marple case concerned the valuation of a 200,000 square foot shopping center subject to a 75-year lease at a constant rent of \$1.47 per square foot. In the assessment trial, the taxpayer presented an appraisal using the actual rent generated by the lease, whereas the taxing districts used market rent. The case was appealed all the way to the Pennsylvania Supreme Court which defined the issue in the case as to whether contract rent or market rent should be used to arrive at the "actual value" for real estate taxation. In its ruling in favor of the taxpayer, the Marple Court issued the oft-cited rule that the "economic realities," of the property, i.e., the contract rent must be considered in valuation.

For twenty years, Pennsylvania's lower courts, assessors and practitioners on both the taxpayer and taxing district sides interpreted Marple to mean that, for leased real property, just the leased fee interest should be valued for tax assessment purposes. In practice, this meant that properties across one class – for example, retail properties – were being taxed unevenly depending on how their leases were structured.

WHERE WE ARE: THE FACTS OF TECH ONE

In Tech One, the taxpayer challenged the \$30 million assessment of a 400,000 square foot shopping center in the suburbs of Pittsburgh. The center sits on 50 acres of land, which is leased to the tenant, Tech One Associates, at a flat rent of \$665,000 for a 50-year term. The tenant constructed the improvements, from which the landlord received no income. At trial, taxpayer interpreted Marple to mean that only the leased fee interest needed to be valued, and entered into evidence an appraisal of the leased fee interest at \$9.5 million. The taxing districts, on the other hand, asked their appraiser to value both the leased fee interest and the leasehold interest; their appraiser opined values of \$9.3 million for the leased fee and a range of \$22 million to \$36 million for the leasehold, and then aggregated to arrive at a total value. Because the appraisers essentially agreed on the leased fee value, the issue in the case was whether or not the leasehold interest should be valued.

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Ideas for You

CHECK THE TIME BEFORE YOU CRITICIZE

It's not only *what* you say and *how* you say it that you must consider; it's also *when* you say it. You can praise a employee any time and it will always be welcome. But before you offer criticism, ask yourself: *Is this the best time?*

If an employee is up to his elbows in a complicated task or project, let him finish. If an employee is about to leave on a three-day weekend, wait until she gets back. You want the individual to accept the criticism and use it to improve performance. Yet in each of the examples cited, your input will likely become a momentary distraction - and a lasting morale-killer. Choose a time when the employee can fully concentrate on what you have to say.

HOW FAR WILL YOU BEND?

Before meeting with employees to kick off a new project or initiative, you should have an idea in your head of the schedule you want. But don't get locked into it. What seems realistic to a manager might seem outrageous to the people who actually do the work. So go to the meeting with *two* dates in your head: the one you want and the one you can live with. If you're not willing to bend, you employees will view you as unreasonable. And the more you work with them, the better they will work for you.

Adapted from Communication Solutions.

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The trial court ruled in the taxing districts' favor, deciding that both leased fee and leasehold interests must be valued. The Commonwealth Court affirmed. The Supreme Court took the case and heard oral argument on April 13, 2011. The issue in the Tech One case was whether the leasehold must be valued. On April 25, 2012, the Supreme Court issued a 34-page opinion, ruling that "[w]here ... ownership of taxable real estate which comprises one tax parcel is divided into leased fee and leasehold interests, [the statute] still requires that the market value of the real estate as a whole be determined." Tech One at 31. In so holding, the Court cited its own prior decisions stating that real estate to be assessed "means the entire property and not merely its constituent elements," North Park Village, 184 A.2d 253 (Pa. 1962) (emphasis in original), and "[e]vidence presented must be directed to the market evidence as a whole," Rieck Ice Cream, 209 A.2d 383 (Pa. 1965). The Supreme Court reconciled Marple by pointing out that Marple did not preclude valuation of the leasehold interest, and further that Marple's requirement to consider the economic realities of the contract rent remains good law. Presented with the valuation evidence entered in the Tech One case, the Supreme Court approved the taxing


district's methodology of arriving at the value of the whole by aggregating the leased fee and leasehold interests. An interesting footnote that did not become evidence in the trial because it occurred afterwards is that post-trial Tech One Associates sold its leasehold interest for approximately \$18 Million.

WHERE WE ARE HEADED: CONSTITUTIONAL UNIFORMITY

The Tech One Court ruled that all interests in leased real property must be valued and added together to arrive at the actual market value on which the property should be assessed and taxed. In so doing, the Court moved Pennsylvania closer to the rule in most other states which value the fee simple, or the entirety of the rights in a piece of property, when valuing properties for taxation. In an assessment appeal, evidence of leased fee and leasehold values should be prepared for leased properties. Because, as a practical matter, assessors frequently do not have access to the lease, assessors can arrive at the value of the whole by using a fee simple approach. On a practical level, Tech One will result in the taxing of leased real property on a more uniform basis, by valuing all properties on the

same basis regardless as to how the ownership interests may be divided and, thus meeting Pennsylvania's Constitutional requirement of uniformity in taxation.

Sharon F. DiPaolo is a partner with Siegel, Siegel, Johnson & Jennings, Co., L.P.A. and manages the firm's Pennsylvania practice. She concentrates her practice in representing commercial taxpayers on property tax issues. The firm is a founding member of the American Property Tax Counsel (APTC), a nationwide group of property tax attorneys with local relationships and expertise, serving taxpayer needs throughout the United States and Canada. Ms. DiPaolo represents taxpayers in assessment appeals throughout Pennsylvania's 67 counties at the administrative, trial court and appellate levels.



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