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Self Constructed Assets

TO: Assessors & Equalization Directors
FROM: State Tax Commission

RE: **REPORTING AND VALUATION OF SELF-CONSTRUCTED ASSETS**

The State Tax Commission has recently become aware of the fact that some companies may not be reporting all of the costs associated with the production of self-constructed personal property assets. Self-constructed personal property assets are those assets which a company constructs on its own or which it hires subcontractors to construct while supervising the construction project itself.

Article IX, Section 3 of the State Constitution requires that assessments shall be uniform (except for certain changes related to Proposal A passed by the voters on March 15, 1994.) It is therefore required that assets which are self-constructed shall be assessed uniformly with similar assets which are purchased, completely-constructed, from a company which sells those assets at the retail level of trade. In other words, a company which self-constructs assets for its own use, should not receive a lower assessment than other similar assets because of a failure by the owner of the self-constructed assets to report the various costs associated with the production of a self-constructed asset including direct and indirect costs.

As a general policy statement, the appropriate costs to be included by an owner of self-constructed assets are all of those costs which a vendor of completely-constructed assets would include when determining a price to charge for its product on the retail market. These costs include direct costs and indirect costs. The following is a listing of the types of direct and indirect costs which shall be included. This list is taken from pages 346 and 347 of The Appraisal of Real Estate, 11th Edition.

Direct Costs

> *Direct costs are expenditures for the labor and materials used in the construction of improvements.* The overhead and profit of the general contractor and various subcontractors are part of the usual construction contract and, therefore, represent direct costs that should always be included in the cost estimate. Direct costs also include the cost of:

- Building permits
- Materials, products, and equipment
- Labor used in construction
- Equipment used in construction
- Security during construction
- Contractor’s shack and temporary fencing
- Material storage facilities
- Power line installation and utility costs
- Contractor’s profit and overhead, including job supervision; worker’s compensation; and fire, liability, and unemployment insurance
- Performance bonds

Indirect Costs

Indirect costs are expenditures or allowances that are necessary for construction, but are not typically part of the construction contract. Indirect costs may include:

- Architectural and engineering fees for plans, plan checks, surveys to establish building lines and grades, and environmental studies
- Appraisal, consulting, accounting, and legal fees
- The cost of carrying the investment in land and contract payments during construction (If the property is financed, the points, fees or service charges, and interest on construction loans are indirect costs.)
- All-risk insurance expense and ad valorem taxes during construction
- The cost of carrying the investment in the property after construction is complete, but before stabilized occupancy is achieved
- Supplemental capital investment in tenant improvements or leasing commissions
- Marketing costs, sales commissions, and title transfers
- Administrative expenses of the developer
- The cost of title change

While some of the items listed above are specific to real property, the list does indicate the types of costs which shall be reported. An assessor or taxpayer who questions whether a particular cost should be reported may seek clarification from the State Tax Commission.

Important Note: If a taxpayer fails to report all of the costs that apply to self-constructed assets, this under-reporting will result in omitted property as defined in Section 34d of the General Property Tax Act (assuming that the assessor appraises the property by applying the STC Personal Property Multipliers to the under-reported costs). Therefore, the discovery of this under-reporting will result in an "addition" in the Capped Value formula. An addition in the Capped Value formula will further result in an increase in Taxable Value over and above the cap of 5% or the rate of inflation (whichever is less).