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Revenue and Transportation Interim Committee

60th Montana Legislature

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TO: HB 488 Subcommittee

FROM: Jeff Martin, Legislative Research Analyst

SUBJECT: Review of Property Valuation in Selected States

Except for Montana and Maryland, local assessors or appraisers value property for property tax purposes. In Montana and Maryland, the state is responsible for the valuation of all property. State tax agencies generally value utility property, railroads, and property that crosses county lines (e.g., pipeline property). The purpose of this memorandum is to review property valuation methods in selected states (Colorado, Oregon, Maryland, Michigan, Utah, and Florida). State tax agencies typically have some supervisory function over county assessors, particularly for ensuring uniformity and equalization.

COLORADO[1]

Real property in Colorado is reappraised every 2 years by local assessors. The property value, or actual value, reflects the appropriate base year level of value. For assessment years 2007 and 2008 the base period is the 18-month period from January 1, 2005, through June 30, 2006. Market data, including sales and rents and expenses for commercial property, is collected during the base period to project values for the 2007 and 2008 period. January 1 is the assessment date.

The market approach (sales), cost approach (replacement cost, less depreciation), and income approach (capitalized net income) may be considered in determining the value of property. The Colorado Constitution (Amendment 1) requires that the market approach be used to value all residential property. Market sales of similar property occurring in the base period are analyzed, compared, and adjusted for time (to June 30, 2006) to determine the value of property.

[1] "2007 Reappraisal: Real Property Summary," Prepared by the Assessment Division, City and County of Denver, May 2007.

Generally, actual value is based on the one approach that most accurately reflects market value. However, some classes of property, such as commercial or industrial property, may be valued by correlating two or three approaches.[2]

For the current reappraisal cycle, the assessor estimated the fair market value of all real property as of June 30, 2006, based on the condition of the property on the January 1, 2007, assessment date. A variety of factors are considered in the valuation of property, including inflationary trends, the value of new construction, remodeling, renovation, demolition, change in use, or any other component of the real estate market.

The nominal assessment ratio of residential property is 21% of market value. However, the Colorado Legislature must adjust the ratio to insure that the percentage of the aggregate statewide value of property attributable to residential property remains the same as in the previous tax year.[3] The residential ratio is adjusted to maintain the residential percentage of total taxable value at 45%.[4] The assessment ratio for residential property in 2007 and 2008 is 7.96%. The assessment ratio for all other property is 29%. Amendment 1 provides that taxing jurisdictions may only increase mill levies to account for inflation and local growth or to recover revenue because of tax abatements or refunds. The electorate must approve any other increases in mill levies.

OREGON[5]

Real property in Oregon is revalued every year by county assessors. Property is valued at 100% of its real market value as of January 1 and is assessed at the lesser of real market value or maximum assessed value (the value taxed is the called the assessed value). Real market value is the value at which the property would change hands between a willing buyer and a willing seller. The initial value of real property is determined by a physical inspection and a comparison of sales data from similar property. For succeeding tax years, the value of the property may be updated based on trends of similar property.

Maximum assessed value is an odd duck.[6] For the tax year beginning July 1, 1997, the maximum assessed value of existing property is the property's real market value for the tax year beginning July 1, 1995, reduced by 10 percent. The maximum assessed value of new property is equal to

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[2] Section 15-8-111(2)(b), MCA, provides that "[i]f the department uses the capitalization-of-net-income method as one approximation of market value and sufficient, relevant information on comparable sales and construction cost exists, the department shall rely upon the two methods that provide a similar market value as the better indicators of market value."

[3] State Tax Guide, Commerce Clearing House, Inc., 2007.

[4] Joan M. Youngman, "The Variety of Property Tax Limits: Goals, Consequences, and Alternatives", State Tax Notes, Vol. 46, No. 8, (November 19, 2007), p. 546.

[5] "Real Property Assessment and Taxation", Information Circular, Oregon Department of Revenue, February 2004.

[6] The concept of maximum assessed value was adopted as a constitutional referendum (Measure 50) by the Oregon electorate in 1997.

the real market value of the property times the ratio of average maximum assessed value to average real market value of similar property in the same property class in the area in which the new property is located. For tax years beginning on or after July 1, 1998, the maximum assessed value is the greater of 103% of the property's assessed value from the prior year or 100% of the property's maximum assessed value from the previous year. This means that the maximum assessed value will increase by 3% a year unless the real market value of the property is less than the maximum assessed value for two years in a row. If that happens, the maximum assessed value will not increase in the second year.

There is little or no connection between market value and the assessed value of real property in Oregon. Assessed value is based on an historical value with some adjustment. The break between market value and assessed value has dismayed some Oregon property taxpayers. For example, one taxpayer successfully challenged the real market valuation of the taxpayer's property and expected a reduction in taxes, particularly after demonstrating that three superior houses had lower assessed values.[7] However, the Oregon Tax Court disabused the taxpayer of the notion that taxes were proportional to market value or to taxes assessed on comparable property.[8] In addition, there is no reassessment of property on change in ownership. For example, one couple was stuck with a previously established maximum assessed value even though they paid much less than the real market value of the property that had been determined 2 years earlier. The Oregon Tax Court found that a "subsequent owner is not able, under Measure 50, to revive the appeal rights available to their predecessor."[9]

The idea of uniformity and equalization of property values is irrelevant under Measure 50. In the first case mentioned above, the Tax Court notes that the former name of the current Board of Property Tax Appeals was the Board of Equalization.[10]

MARYLAND[11]

Article 15 of the Declaration of Rights of the Maryland Constitution requires that all property be assessed and taxed uniformly. Like Montana, the state is responsible for the appraisal and equalization of the valuation of property subject to taxation. Property is assessed on the basis of fair market value. The Maryland Department of Assessments and Taxation appraises real

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[7] Youngman, *op. cit*, p. 549.

[8] *Ibid.* p. 549.

[9] McCollum v. Multnomah County Assessor, Oregon Tax Court Magistrate Division, Property Tax (Nov. 18, 2005). Quoted in Youngman, p. 550.

[10] MeKee v. Clackamas County Assessor, Oregon Tax Court Magistrate Division, Small Claims, Property Tax (Nov. 18, 2005).

[11] "A Homeowner's Guide to Property Taxes and Assessments", Maryland State Department of Assessments and Taxation.

property every 3 years.[12] An increase in value is phased in equally over the 3-year cycle. Real property is assessed at 40% of its phased-in value.

Assessors use the sales (market) approach and cost approach (construction costs, less depreciation for age and condition of the improvement) to estimate the fair market value of residential improvements and the sales approach to value residential land. The value of improvements is estimated using the cost approach with a market value index adjustment if sales of similar properties indicate that a particular style of home is worth more or less than the cost approach.

Income producing property may be valued by using the capitalization of net income approach or any other appropriate method (Section 8-110, Property Tax Article, Maryland Code).

MICHIGAN[13]

In 1994 Michigan voters approved a measure to increase that sales and use tax by 2 percentage points and to cap the rate of the annual increase in taxable value of each parcel of property to the rate of inflation or 5%, which ever is less.

Property subject to taxation in Michigan is classified as either real or personal property. Real property includes agricultural, commercial, developmental, industrial, residential, and timber cutover. All property is assessed uniformly at 50% of "true cash value". Property is assessed annually. First, the local assessor determines the assessed value of property based on the condition of the property on December 31 of the previous year.[14] Second, the board of commissioners applies an adjustment factor to the assessments of each city and township in which assessments are above or below the required level. Finally, the Michigan Tax Commission applies an adjustment factor to the assessments of a county when its assessments, after the county adjustments, fail to meet the required level. The result is the state equalized valuation. The calculation is made for each class of property.

Taxable value is the basis for property taxation in Michigan. Each parcel of property has a state equalized valuation and a taxable value. If the true cash value of a property rises faster than the rate if inflation or 5%, whichever is less, the property's taxable value (adjusted for deletions or additions to the property) may grow at a rate that is much lower than the growth rate for the state equalized value. When property changes hands, the previous year's state equalized value becomes the property's taxable value. The change to state equalized value does not apply to agricultural land if a purchaser of eligible farmland files an affidavit that the land will be used for agricultural purposes for seven years.

[12] Railroad property and public utility property is valued annually.

[13] "Michigan Taxpayer's Guide", prepared by the Michigan Legislature with the assistance of the Michigan Department of Treasury, January 2008.

[14] The appraisal of property may be contracted to private appraiser.

UTAH[15]

In Utah, residential and commercial property is appraised by local (county) assessors. An assessor divides the county into "model areas" for reappraisal. Approximately one-fifth of residential property in the county is reappraised every year. If significant changes have occurred in a particular area, the reappraisal of the area may be accelerated. Assessors gather information on the physical characteristics of the property as well as replacement cost information. Information may be gathered by an on-site inspection or by using pictometry.(oblique aerial photography). The assessment of other residential property is determined by annual sales assessment ratio studies based on neighborhood, property type, and other characteristics.

Business real property is also subject to reappraisal every five years. However it may be reappraised by property type (apartments, commercial property, industrial property, office buildings). In rural counties, all commercial property may be reappraised in a single year. If enough sales information is available, a sales assessment ratio study is used to update assessments on other business property. If there are insufficient sales, a fee appraiser or the Utah Tax Commission may provide advice.

The Utah Tax Commission evaluates the assessment performance of local assessors to determine the equity and uniformity of property assessment within each county.[16] If assessments in a county vary by more than 10% of market value, the Commission may issue corrective orders to the county assessor.

Residential property (vacation homes, cabins, time-shares, and other types of transitory housing do not qualify as residential property) is taxed at 55% of market value, and all other types of property are taxed at 100% of market or assessed value.

FLORIDA

The property tax in Florida is a local tax administered by local officials. County property appraisers are local elected officials responsible for determining the market value of all property within their respective county. Property is reappraised annually. County appraisers use the market approach, replacement cost approach, and net income approach to value property. A county may have a computer assisted mass appraisal system to incorporate all three approaches, if applicable. The market approach using sales data from the previous year may be the best indicator of market value.[17] Property appraisers review changes in property values in the county and market-area variations in value. They conduct on-site inspections of property and gather data on building permits, sales, and other market indicators. The information is used to determine initial assessed values for all property in the county.

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[15] Phone conversation with Joy Jasperson, Utah State Tax Commission, Property Tax Division, April 9, 2008.

[16] "2007 Assessment/Sales Ratio Study: For Sales Occurring January 1, 2006, to December 31, 2006", Utah Tax Commission, Property Tax Division.

[17] Alachua County Property Appraiser at http://www.acpafl.org/faq.html.

Although property is locally assessed, the Florida Department of Revenue plays a significant role in determining the uniformity and accuracy of the local assessments.[18] Every 2 years the Department analyzes sales data and conducts on-site appraisals of sample property within a county. The Department compares the sample property values with the values determined by property appraisers on the same property. Based on the results of the Department's analysis the local property appraiser may revise the assessment roll. The Department is required to approve each county's assessment roll. If the Department does not approve the roll, the county uses the prior year's assessments until the new roll is approved.

In 1992, Florida voters approved Amendment 10 to the Florida Constitution to limit the amount of increase in the assessed value of residential homestead property to the lessor of 3% or the rate of inflation. The amendment went into effect in 1995. The assessment limit does not apply to additions or renovations to the property in the year the new property is taxable. However, the property is included in the assessment cap in subsequent years. The assessed value may not exceed the market value of the residence. If the ownership of residential property changes, the property would be valued at market value and the assessment cap would apply in subsequent tax years.

In 2007, the Florida Legislature referred SJR 2D (Amendment 1) to the electorate to amend the state's constitution to expand the assessment limits. The amendment expanded the homestead exemption from $25,000 to $50,000 (the increased exemption amount does not apply to school levies) and allowed residential property owners to transfer up to $500,000 of the difference in the market value and assessed value of the previous homestead to a new homestead. Homestead property owners are also allowed to transfer a portion of the assessment limit to another homestead with a lower market value. One of the reasons for allowing "portability"of the assessment limits was to allow residents to keep a portion of the property tax cap when they purchased a new home.

The amendment also provided a 10% limit on the increase in assessed value for other residential property and business real property, except for school levies, and a $25,000 exemption for business personal property.

CONCLUSION

The assessment of property for tax purposes is seemingly more efficient at the state level. It eliminates the need for state tax agencies to verify, approve, and equalize valuations determined at the local level. Every state, except Maryland and Montana, values most property locally. It may be that taxpayers local assessment states have a higher level of confidence in local people doing the job. One change the subcommittee might want to consider is revising the reappraisal cycle or changing the date when new values go into effect.

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[18]"Property Tax Oversight Program", Florida Department of Revenue, January 2008.