



Mike Kadas
Director

Montana Department of Revenue

EXHIBIT /
DATE 4/13/15
SB 157



Steve Bullock
Governor

MEMORANDUM

TO: Mike Miller, Chairman, House Taxation Committee
FROM: Mike Kadas, Director, Department of Revenue
DATE: April 13, 2015
RE: Senate Bill 157 – Hearing Requests

The department is providing the following information in response to questions and requests during the House Taxation hearing held on April 8, 2015:

Analysis of Mr. Joe Roberts' (Montana Association of Realtors) handout.

Mr. Roberts reviewed the department's website and determined that under SB 157 that the total taxes for a median home value will increase between TY2014 and TY2015 by 4.12%. This is correct, however it ignores that under current law total taxes for the median home are estimated to increase by 5.62%. Mr. Robert's also estimates the mills in his example at 631, while the department estimates the mills at 605. This appears to be a copying error in that, the overall taxes seem to match the department's estimates. Mr. Roberts testified that the department is eliminating the homestead exemption. This is inaccurate. The overall rate for residential property in TY 2014 is not 2.47%, as stated in 15-6-134, MCA, but rather 1.31% ($2.47\% \times (1-47\%)$) as a result of the homestead exemption. Taking the homestead exemption factor into account, the rate will change from 1.31% to 1.35% in SB 157, which is the taxable value neutral adjustment, but an increase of 3% in taxable value for residential property.

Forest Land.

Capitalization rates and stumpage values effect on forest land valuation; Interest Rates on Farm Loans, and Similarities to Agricultural Land. See Attached.

Minimal updates required for a 2-year reappraisal. The reappraisal of forest lands every two years requires an update of stumpage values, forest costs, and agricultural income by dropping the 2 earliest years and adding the 2 most recent years to calculate a 10-year average. Additionally, the department's forest productivity model is developed and readily available with no updates required.

Tax rate for homes over 1.5 million.

A residential property with a market value of \$17,784,287 will receive a general tax obligation under current law in the amount of \$112,080. Under SB157, this same

residential property with a market value of \$17,784,287 will receive a general tax obligation in the amount of \$90,050 or 19.65% lower than current law. Under current law 15-6-222(1)(b), the homestead exemption is applied only to the first \$1.5 M in improvement value of a single – family residential dwelling. The improvement value above \$1.5M is taxed at 2.47%. Proposed law (SB 157) would tax the same improvement value at 1.89%.

Elimination of Extended Property Tax Assistance Program (EPTAP).

For the 2009-2014 reappraisal cycle, the department mailed approximately 177,000 applications, approximately 15,000 property owners qualified and received an average reduction of \$290 on their tax bill. For the 2015 reappraisal cycle, the department estimates mailing approximately 18,000 applications. The number of qualified applicants is expected to be significantly lower, similar to the prior cycle.

Based on the Montana Housing Price Index, housing prices have on average grown by 3.5% since 1980. Under a normal 6-year reappraisal cycle, home prices could be expected to increase on average by 22.9%. During this reappraisal cycle on average home prices in Montana declined by 2.85%. The first criterion for a home to be eligible for EPTAP is that its value needs to increase 24%, 30%, or 36% higher than the statewide average. For a home to be eligible for EPTAP their increase would need to be 21.15% (24%-2.85), 27.15% (30%-2.85%), and 33.15% (36%-2.85%). In a normal cycle ETAP would apply to homes that saw an increase of 46.9% (24%+22.9%), 52.9% (30%+22.9%), or 58.9% (36%+22.9%). In the last cycle to qualify, you needed increase of 80% (24%+56%), 86% (30%+56%), or 92% (36%+56%).

Gallatin County FTE

Over the past two reappraisal cycles, the Department has regularly, but temporarily shifted FTE from other counties to Gallatin County to assist mostly with picking up new construction. On an annual basis, this has amounted to the equivalent of between 1 and 2 FTE per year, depending on the workload. This has been necessary primarily to deal with the rapid growth experienced in Gallatin County.

**Similarities Between
Agricultural Land Valuation and
Forest Land Valuation**

Agricultural Land	Forest Land
2 Years	2 Years
Productive Value based on the land's potential to grow a crop annually	Productive Value based on the land's potential of annual forest growth
A 10 year Olympic average of agricultural prices	A 10 year average of stumpage values
A 25% crop share or operating expense to account for cost of owning the land	A 10 year average of forest cost expenditures supplied by DNRC, and a 25% operating expense on grazing

Interest Rates on Farm Loans

Average effective interest rates on new loans under Farm Credit Services

YEAR	INTEREST RATE
2009	6.17%
2010	6.41%
2011	6.12%
2012	5.61%
2013	5.55%
5 Year Average	5.97%

Interest Rate	5.97%
Effective Tax Rate	+0.14%
Capitalization Rate	6.11%

*IRS Bulletins 2009-21, 2011-17, 2012-39 at www.irs.gov/irb and www.e-farmcredit.com

Effects of Changing Stumpage Value and Cap Rate

Example of How Changing Stumpage Value and Cap Rate Effects the Value of an Acre of Forest Land

	Productivity @ BF/acre	x	Stumpage Value	=	GI/acre	-	Forest costs + ag income	=	Total Income	+	Cap rate	=	Productive Value/Acre
TY 2014	260.75	x	\$0.33	=	\$86.04	-	\$11.00	=	\$75.04	+	8.0%	=	\$938.00
TY 2015 Current Law	260.75	x	0.1824	=	\$47.56	-	\$11.00	=	\$36.56	+	8.0%	=	\$457.01
Change Cap Rate	260.75	x	0.1824	=	\$47.56	-	\$11.00	=	\$36.56	+	6.4%	=	\$571.26
Change Stumpage Value	260.75	x	0.2233	=	\$58.22	-	\$11.00	=	\$47.22	+	8.0%	=	\$590.25
SB 157	260.75	x	0.2233	=	\$58.22	-	\$11.00	=	\$47.22	+	6.4%	=	\$737.81

Calculation of Taxable Value Neutral Tax Rate for Selected Scenarios

Class 10 Forest Value Mitigation Options						
	TY 2014	Current Law	Change Cap Rate	Change Stumpage Value	SB157	
Stumpage Value Period	5 Year	5 Year	5 Year	10 Year	10 Year	
Capitalization Rate	8.00%	8.00%	6.40%	8.00%	6.40%	
Market Value (Millions)	\$2,155.93	\$1,088.98	\$1,386.43	\$1,365.06	\$1,696.92	
Mitigated Rate	0.29%	0.29%	0.45%	0.46%	0.37%	
Taxable Value (Millions)	\$6.25	\$3.16	\$6.25	\$6.25	\$6.25	
Average Mills for Forest Land*	486.80	516.06	495.76	495.76	495.76	
Estimated Taxes (Millions)	\$3.04	\$1.63	\$3.10	\$3.10	\$3.10	
*Reflects an estimated increase in mill levies of 6% under current law and 1.84% under proposed law						

Current Law and SB 157's Treatment of Homes with Improvement Value Greater Than \$1.5 Million

Example of How the Homestead Exemption Cap Works									
Current Law									
	Market Value		Actual Tax Rate		Taxable Value		Mill Levy		General Tax
Land	\$ 2,787,942	x	1.31%	x	\$ 36,522	x	0.28773	=	\$ 10,508
Homestead	\$ 1,500,000	x	1.31%	x	\$ 19,650	x	0.28773	=	\$ 5,654
No Homestead	\$ 13,496,345	x	2.47%	x	\$ 333,360	x	0.28773	=	\$ 95,918
Total Imps	\$ 14,996,345		-		\$ 353,010	x	0.28773	=	\$ 101,571
Total	\$ 17,784,287				\$ 389,532				\$ 112,080
Proposed Law SB 157									
	Market Value		Tax Rate		Taxable Value		Mill Levy		General Tax
Land	\$ 2,787,942	x	0.0135	x	\$ 37,637	x	0.28773	=	\$ 10,829
Homestead	\$ 1,500,000	x	0.0135	x	\$ 20,250	x	0.28773	=	\$ 5,827
No Homestead	\$ 13,496,345	x	0.0189	x	\$ 255,081	x	0.28773	=	\$ 73,394
Total Imps	\$ 14,996,345		-		\$ 275,331	x	0.28773	=	\$ 79,221
Total	\$ 17,784,287				\$ 312,968				\$ 90,050

Current Law Rates & Exemptions, 2015 Values Fully Phased-In

Property Type	2014 Market Value	2015 Market Value	Percent Change in Value	Exemption Rate	Tax Rate	Actual Tax Rate	2015		2014		Change in Taxable Value
							Taxable Value	Tax Rate	Taxable Value	Tax Rate	
Agricultural	\$5,467,386	\$6,381,551	16.72%	-	2.47%	2.47%	\$157,624	2.16%	\$143,897	2.16%	\$13,727
Residential	\$89,778,076	\$87,218,359	-2.85%	47.00%	2.47%	1.31%	\$1,141,776	1.35%	\$1,168,360	1.35%	-\$26,584
Commercial	\$18,294,152	\$18,742,568	2.45%	21.50%	2.47%	1.94%	\$363,409	1.89%	\$350,605	1.89%	\$12,804
Forest	\$2,128,925	\$1,059,694	-50.22%	-	0.29%	0.29%	\$3,073	0.37%	\$6,252	0.37%	-\$3,179

Taxable Value Neutral Rates & Exemptions, 2015 Values Fully Phased-In

Property Type	2014 Market Value	2015 Market Value	Percent Change in Value	Exemption Rate	Tax Rate	Actual Tax Rate	2015		2014		Change in Taxable Value
							Taxable Value	Tax Rate	Taxable Value	Tax Rate	
Agricultural	\$5,467,386	\$6,381,551	16.72%	-	2.16%	2.16%	\$143,897	2.16%	\$143,897	2.16%	\$0,000
Residential	\$89,778,076	\$87,218,359	-2.85%	37.50%	2.16%	1.35%	\$1,168,360	1.35%	\$1,168,360	1.35%	\$0,000
Commercial	\$18,294,152	\$18,742,568	2.45%	12.50%	2.16%	1.89%	\$350,605	1.89%	\$350,605	1.89%	\$0,000
Forest	\$2,128,925	\$1,059,694	-50.22%	-	0.59%	0.59%	\$6,252	0.59%	\$6,252	0.59%	\$0,000

SB 157 Taxable Value Neutral Rates & Multiplier, 2015 Values Fully Phased-In

Property Type	2014 Market Value	2015 Market Value	Percent Change in Value	Multiplier	Tax Rate	Actual Tax Rate	2015		2014		Change in Taxable Value
							Taxable Value	Tax Rate	Taxable Value	Tax Rate	
Agricultural	\$5,467,386	\$6,381,551	16.72%	-	2.16%	2.16%	\$143,897	2.16%	\$143,897	2.16%	\$0,000
Residential	\$89,778,076	\$87,218,359	-2.85%	-	1.35%	1.35%	\$1,168,360	1.35%	\$1,168,360	1.35%	\$0,000
Commercial	\$18,294,152	\$18,742,568	2.45%	1.4	1.33%	1.89%	\$350,605	1.89%	\$350,605	1.89%	\$0,000
Forest	\$2,128,925	\$1,059,694	-20.29%	-	0.37%	0.37%	\$6,252	0.37%	\$6,252	0.37%	\$0,000