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Revenue and Transportation Interim Committee

61st Montana Legislature

SENATE MEMBERS

KIM GILLAN--Chair
RON ERICKSON
JEFF ESSMANN
CHRISTINE KAUFMANN
JIM PETERSON
BRUCE TUTVEDT

HOUSE MEMBERS

ROY HOLLANDSWORTH--Vice Chair
DICK BARRETT
CYDNIE (CARLIE) BOLAND
BRIAN HOVEN
MIKE JOPEK
BILL NOONEY

COMMITTEE STAFF

JEFF MARTIN, Research Analyst
LEE HEIMAN, Staff Attorney
FONG HOM, Secretary

MINUTES

Residential and Commercial Property Reappraisal Subcommittee

August 2, 2010

Room 137, Capitol Building
Helena, Montana

Please note: These minutes provide abbreviated information about committee discussion, public testimony, action taken, and other activities. The minutes are accompanied by an audio recording. For each action listed, the minutes indicate the approximate amount of time in hours, minutes, and seconds that has elapsed since the start of the meeting. This time may be used to locate the activity on the audio recording.

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COMMITTEE MEMBERS PRESENT

REP. DICK BARRETT

SEN. KIM GILLAN
SEN. JEFF ESSMANN
SEN. CHRISTINE KAUFMANN
SEN. BRUCE TUTVEDT

COMMITTEE MEMBERS EXCUSED

REP. BILL NOONEY

STAFF PRESENT

LEE HEIMAN, Staff Attorney
FONG HOM, Secretary

Visitors

Visitors' list, Attachment #1.

COMMITTEE ACTION

CALL TO ORDER AND ROLL CALL

- 00:00:01 REP. BARRETT called the meeting to order at 8:04 a.m. The secretary noted roll visually. REP. NOONEY was excused.
- 00:00:26 The minutes of the April 29, 2010, subcommittee meeting were approved as read with a correction to the subcommittee members present, SEN. ERICKSON was not at the meeting.

AGENDA

- **STATUS OF AB 26 REVIEW AND TAX APPEAL - Cynthia Monteau Moore, Department of Revenue**

- 00:01:53 Ms. Moore introduced the regional managers of the newly formed regions: Larry Richards, Regional Manager for Region III; Scott Williams, Regional Manager for Region I; and Rocky Harrelson, Regional Manager for Region IV.
- 00:04:21 Ms. Moore discussed the status of the AB 26 appeals in the four regions found in the Department of Revenue's Reports (**Exhibit 1**).

Questions

- 00:08:02 SEN. TUTVEDT asked when the AB 26s will be done in the Flathead and Lake Counties? **Ms. Moore** said that the Department of Revenue has a limited number of appraisal staff and each review takes four hours to complete.
- 00:09:02 SEN. TUTVEDT asked if the Department is anticipating moving more resources to help with the AB 26 appeal process? **Ms. Moore** said that the Department is trying to get local appraisers to help. **Scott Williams, Regional Manager for Region I**, said that the Department staff presents the information to the taxpayer, and the taxpayer has the opportunity to discuss that information and that communication between the reviewer and the taxpayer takes three to four hours.

Public Comment

None at this time.

- **DECLINING POST-APPRAISAL RESIDENTIAL PROPERTY VALUES**

- **Valuation Trends in Flathead County - Jim Kelley, Appraiser**

- 00:22:42 Mr. Kelley gave a presentation on valuation trends on Flathead, Lake, and

Missoula Counties in the last three years.

Questions

- 00:39:25 SEN. GILLAN said that Mr. Kelley has access to the sales data because he is an appraiser, so it is not information on the listed price of the property. **Mr. Kelley** said that it is the actual sales price but doesn't represent 100% of the sales.
- 00:40:55 SEN. GILLAN said that early on in the discussions, there was a concern in the Flathead that the property reappraisal values were off the mark. As she looks at Mr. Kelley's information for 2008, it seems to her that some of his data indicated that the Department of Revenue was on the right track in terms of the value. **Mr. Kelley** said that he agrees with that but he would have liked to have seen entire groups because there are outliers on both sides.
- 00:43:13 REP. BARRETT asked if Mr. Kelley has reviewed the sales assessment ratios studies that the Department of Revenue has done? **Mr. Kelley** said that he has.
- REP. BARRETT asked if his results from Flathead County generally conformed with those results? **Mr. Kelley** said that the problem was that the Department of Revenue took data from 15 months prior to July 1, 2008, and then 15 months after July 1, 2008. They didn't restrict it to one year, resulting in increased values on one side of that time period and a decrease of values on the other side. Their conclusion came out on that study was right based on how they handled their data.
- 00:46:19 REP. BARRETT asked, if he made the comparison of actual sales values in 2004 to the Department's assessed values in 2002, would they have been higher? **Mr. Kelley** said that he couldn't answer that because he didn't look at 2004. Property values during that time period were increasing so it is reasonable to conclude that the Department of Revenue's value would have been lower than what the actual market value was in 2004.
- 00:47:23 SEN. KAUFMANN said that Mr. Kelley talked about removing some outliers based on the amount of acreage. Were there other kinds of outliers that you removed, for example, arm's length sales, or were they automatically excluded because of your data set? **Mr. Kelley** said that he wouldn't have any knowledge of that, so those wouldn't have been removed.
- 00:48:37 SEN. ESSMANN asked Mr. Williams how many residential neighborhoods in Flathead County did the Department use in developing the appraisal for the 2008 cycle. **Mr. Williams** said that about 200 residential neighborhoods. There are 5

residential model areas as opposed to neighborhoods.

00:49:39 SEN. ESSMANN said the next step of the analysis would be to separate Mr. Kelley's countywide analysis into analysis for each of those 5 model areas to see if there are enough sales in each of those areas to re-evaluate the model as a whole. **Mr. Williams** said that every market changes differently within a county. You would have to look at those individual market areas to address some of the other issues, making sure all sales are addressed, not just the ones that are MLS, and making sure that arm's length transactions are actually taken into consideration.

00:58:22 SEN. TUTVEDT asked for printed version of Mr. Kelley's presentation.

▶ **Outline of proposed bill draft -- rate change for lost value and adoption of new value upon successful appeal -- Sen. Bruce Tutvedt**

00:59:57 Sen. Tutvedt's outline of his proposed LC 147 was presented by **Lee Heiman, Staff Attorney (Exhibit 2)**.

Questions

01:04:49 SEN. ESSMANN said that this proposal is similar to the EPTAP methodology where each parcel gets a different tax rate. **Mr. Heiman** said the EPTAP is also aimed at the tax rate, and this proposed bill is aimed at the tax rate as opposed to valuation.

01:06:11 SEN. KAUFMANN asked if there was an income test in this bill. **Sen. Tutvedt** said that there is no income test in it, it is just like our property tax system. If your valuation dropped that is what you would get, and if your valuation went up, you would pay more.

01:06:54 SEN. KAUFMANN asked if there was any estimate done about the impact to state revenue base if this plan was put into effect? **Mr. Heiman** said no.

01:07:23 SEN. GILLAN asked if a property was reappraised and then sold, would there be an automatic adjustment for the new owner if the appraised value of the property was less than the appraised value before the property sold? **Mr. Heiman** said that once a property is sold, the new owner continues with how the taxes were determined on his property and an adjustment would only apply to the property that has not changed hands since the base value.

01:10:43 REP. BARRETT said his concern is the issue of uniformity and the treatment of

taxpayers, since this is elective and different taxpayers have different degrees of incentive to make this investment in reappraisal. Another concern is the connection between what you are going after here and the question of phase-in and the frequency of appraisal. The fact of the matter is, that the market value of a property for tax purposes that we use today is actually our best guess of what was happening six years ago. If you consider the charts that Mr. Kelley presented you see the line showing the history of increases over that period. The market value for tax purposes is 6 years old. The fact that they have declined doesn't mean that our guess is any worse. What it does mean is that it is the oddity of only doing this every six years and then phasing it in that we are living six years in the past.

01:14:25 REP. BARRETT asked if Sen. Tutvedt if he was satisfied that there were no constitutional issues in terms of uniformity. **Sen. Tutvedt** said that he and Mr. Heiman talked about that and Mr. Heiman's best guess was that it would be similar to EPTAP.

01:15:26 SEN. ESSMANN said that he does not think that it should be limited to class four residential only. The consensus among the commercial brokers is that class four commercial has suffered general decline in value 15% to 20%. He said that he views this as a proposal for a pressure relief valve on a broiler. It would be preferable to deal with the group affected as discussed by the special subcommittee chaired by Sen. Gebhardt.

01:17:57 SEN. KAUFMANN said that she had a concern about the complexity of the various assistance programs throughout the property tax system and this feels like there will now there will be a fifth assistance program on top of the other four we already have. This one will benefit people with high valued properties and the Department tends to undervalue the high valued properties and we are providing assistance to people who are more able to afford their property taxes. **Sen. Tutvedt** said that this is a fairness issue and it would help those people who are paying more taxes than they should under the system that we have now.

Public Comment

01:22:18 **Irvin Ross, resident of Lake County**, talked about his observations on statistics and the anomaly of sales experienced on Flathead and Lake Counties.

01:28:05 **Gary Wicks, resident of Lake County**, said that a lot of people around Flathead Lake and the other lakes are not from out-of-state, are not wealthy, but people who bought their property in the early 1970s or later or the property was handed

down through generations of Montanans and their basic idea is to try and keep that property and stay in that area as long as they can. This cycle of reappraisal makes it difficult for some of them to do that. The reappraisal system is flawed and does not work on lake front property.

- 01:41:48 **Mark MacDonald, real estate appraiser in Lake County**, said that the Department of Revenue's 2008 snapshot is so far off from the values today. He produced examples of recent sales and discussed them.
- 01:45:13 **Darwin Ernst, appraiser, Hamilton**, felt that two different data sets are being discussed; data from the MLS that is partial disclosure, and data set from the Department of Revenue that is verified sales.
- 01:47:27 **Brian River, resident of Lake County**, said that he is a property owner since 1991, he built his house and is afraid that he will lose his house if he continues to see the kind of property tax increases that he is anticipating.
- 01:50:14 **Jon Brueggeman, Polson**, commented on outliers and the fundamental reason government exists. Montanans have a problem and a huge complicated mechanism which is the Department of Revenue trying to obtain what is the market rate. What has been ignore is the actual market rate. Another problem that has been created is the issue of the county budget that cannot be determined because the counties don't know how much money is coming in after the AB 26s are completed.
- 01:55:46 **Joe Roberts, Montana Realtors Association**, said that Sen. Essmann's description of the need for a pressure relief valve such as this legislation is a very apt one. Mr. Roberts discussed the Montana Supreme Court case entitled Roosevelt which dealt with a long phase-in period.
- 02:01:38 Sen. Tutvedt suggested bringing forward LC 147 and then debate on whether to add commercial. He thinks that we need some hurdle so that we don't have every property owner wanting to have every property revalued. He said he doesn't agree that we should go to a one-year.
- 02:02:29 REP. BARRETT said that there has to be some kind of uniform and universal revaluation process. His reservation about this proposed legislation still stands and the appropriate way to deal with it, is to speed the pace of reappraisal to a one-year basis.

Motion by Sen. Tutvedt

02:04:07 SEN. TUTVEDT moved that the subcommittee recommend LC 0147 for consideration by the full committee with the inclusion of commercial and figure out how to change it at a later date. The motion **passed** unanimously by a voice vote.

BREAK

02:25:15 The meeting reconvened at 10:29 a.m.

• DISCLOSURE OF RESIDENTIAL PROPERTY SALES PRICES

02:25:59 **Darwin Ernest, real estate appraiser, Hamilton**, discussed disclosure and the realty transfer certificate.

02:32:57 **Alan Peura, Department of Revenue**, discussed the report "Public Disclosure of Real Estate Sales Prices" (**Exhibit 1, Tab 3**).

Public Comment

None.

Questions

02:46:47 SEN. GILLAN asked if a realtor automatically has access to the sales price. **Mr. Ernst** said that a realtor has access to the sales data, but they can opt out of showing that sales information with the Multiple Listing Service (MLS) by signing an agreement before you list that property which says you will not disclose the information within the MLS.

02:50:41 REP. BARRETT asked if it is proprietary information belonging to MLS and in order to have access to that proprietary information, you have to be a member. **Mr. Ernst** said that is correct.

02:51:43 SEN. GILLAN asked if the Department of Revenue has to join MLS in order to get that data. **Mr. Peura** said that the Department gets its information from the Realty Transfer Certificates.

Motion by Sen. Gillan

02:53:23 SEN. GILLAN **moved** that staff begin developing a bill draft allowing disclosure on real estate sales.

Discussion

02:56:09 There was a discussion about moving this issue forward. Sen. Essmann said the

suggested language in the memo gives him pause. He thinks that it is in the best interest of the taxpayers for disclosure in order to make a decision about whether to invest the time in the AB 26 process or not. He also thinks there should be a separate bill on class four commercial disclosure.

02:59:30 SEN. GILLAN **withdrew** her motion.

Substitute Motion by Sen. Gillan

SEN. GILLAN **moved** that the committee, in its report, states that there is a recommendation on a bill draft dealing with disclosure with the primary emphasis on residential. The motion **passed** on voice vote.

Motion by Sen. Essmann

03:00:57 SEN. ESSMANN **moved** to recommend to the full committee a bill draft for disclosure on class four commercial and exclude class three and class eight properties. The motion **passed** on voice vote.

• **COMMERCIAL PROPERTY VALUATION -- CRITERIA AND CHOICES FOR PARTICULAR METHODS -- Alan Peura, Department of Revenue**

03:02:35 Mr. Peura gave a presentation on commercial property valuation (**Exhibit 1, Tab 4**).

03:05:47 **Dan Bucks, Director, Department of Revenue**, discussed the issue of commercial property appraisal and the matter of transparency of the choice and the use of the income method.

03:18:12 **Mr. Peura** gave a presentation on the report "Require Commercial Property Tax Owners to Provide Income and Expense Information" (**Exhibit 1, Tab 4**).

03:25:01 **Larry Richards, Regional Manager for Region III**, provided responses to questions on how the process works in the income information of commercial values. (3:37)

Questions on areas of influence

03:37:51 SEN. ESSMANN said Mr. Richards had stated that he had very few sales of property up and down these corridors, but then the Department applied them up and down these corridors through these areas of influence only when you use the cost approach. Is that correct? **Mr. Richards** said they established a land value to all properties. Whenever you do the costs you have to have a land value

and a building value. Land values are applied to these. The difference is, when you do the income approach, then the income rate is applied to the whole property. When we build the models, we don't break out the land itself. We are required by statute to show a value for the building and a value for the land. When we do the modeling for income, it is the property as a whole.

03:44:07 SEN. ESSMANN said that his concern is whether using the cost approach is appropriate for significant percentage of the parcels because what happens in that situation, some of the same area of influence are valued using a cost approach versus an income approach. You basically said that the landlord and the tenant had made a mistake in terms of negotiation of their financial transactions. He didn't think that was logical. **Mr. Richards** said he agrees that the income and the market is the best approach. What he would recommend is that taxpayers look at what would be developed out of the model for income property versus what they sold it for or what they could buy it for versus what the costs comes out.

Questions on capitalization rates

03:50:00 SEN. ESSMANN asked if there were enough sales in the 49 rural counties to separately model a capitalization rate for those counties, or were those extrapolated from urban counties? **Mr. Richards** said that if they had smaller rural communities that were not impacted by Billings or by Laurel, then some of that information would have been put into helping develop the cap rate for the rural areas. They did not use the City of Billings or the City of Laurel to develop a cap rate for the rural counties. But that doesn't say that we did use rural Yellowstone County to help develop cap rates for the other 49.

SEN. ESSMANN said that the cap rates that were developed for rural counties were based upon sales, income, and expense data from those areas plus appropriate rural portions of urban counties.

03:51:10 REP. BARRETT said it is not clear to him why the distinction should be geographic. Has the Department considered developing cap rates based on developing differential cap rates that is based on something other than geography? **Mr. Richards** said that it does seem that it is all geographic, but when you put the information together and start doing the modeling, those counties fell out. Those would be the outliers.

03:53:48 SEN. TUTVEDT asked if cap rates are public knowledge? **Mr. Richards** said that they can provide cap rate information to the public.

03:55:05 SEN. TUTVEDT requested that the Department provide information on cap rates to the committee.

Public Comment

None.

• **ADJOURNMENT**

03:57:38 With no further business before the subcommittee, REP. BARRETT adjourned the meeting at 12:01 p.m.

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