

LEGISLATIVE AUDIT DIVISION

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MEMORANDUM

TO: Legislative Audit Committee Members
FROM: Jeremy Verhasselt, Performance Auditor
CC: Mike Kadas, Director, Department of Revenue
DATE: January 2016
RE: Performance Audit Follow-Up (16SP-11): Property Tax Relief (14P-02)
ATTACHMENTS: Original Performance Audit Summary

Introduction

The *Property Tax Relief* (14P-02) report was issued to the Committee in August 2014. The audit included five recommendations to the Department of Revenue (DOR). In January 2016, we conducted follow-up work to assess implementation of the report recommendations. This memorandum summarizes the results of our follow-up work.

Overview

Audit work determined that the Department of Revenue should improve controls verifying the various requirements for property tax assistance to ensure benefits are administered consistently. Audit work also recommended examining the outreach efforts of the various property tax assistance programs to assess the distribution of benefits across the state. The performance audit contained five recommendations to DOR. Based on the follow up work DOR has implemented or partially implemented all five recommendations.

Background

Property taxes are annual local government taxes on real property based on a tax rate established by the legislature. They are calculated, billed, and collected by local taxing jurisdictions. DOR is responsible for ensuring that all property is treated equitable. Property tax relief is a means to alleviate the property tax burden. This audit looked at three different programs that DOR offers property tax assistance through. These are the Property Tax Assistance Program (PTAP), Disabled American Veterans (DAV), and the Elderly Home Owner/Renter Credit. All three programs are based on income requirements for qualification, with the elderly credit having an age requirement of 62. Those who qualify receive a percentage reduction in their property tax rate based on their income. In 2012 these three tax programs granted \$197,774,143 in property tax relief. The audit largely focused on PTAP and DAV.

Audit Follow-up Results

Our performance audit report contained five recommendations to DOR. As part of the follow-up work, we examined amended administrative rules, reviewed applicable new and amended statutes, interviewed DOR staff, observed documentation related to updated quality assurance processes, and observed the

Orion data system. The Orion system is used by DOR to administer property tax programs. The following sections summarize the progress toward implementation of the report recommendations.

RECOMMENDATION #1

We recommend the Department of Revenue develop and implement additional management tools to improve how they verify the occupancy requirements of the Property Tax Assistance Program.

Implementation Status – Implemented

SB157 that was passed during the last session changed the occupancy requirements. In the report audit staff noted cases in which a real estate transactions showed that an individual had not owned a home for at least seven months, but still received assistance. SB157 changed the occupational qualifications so applicants no longer need to be in the same residence for at least seven months to qualify for property tax assistance. They can now have moved to a different home as long as they resided in the multiple homes for at least seven months. In this situation a qualifying homeowner will receive a reduced property tax rate on only the home they occupy when their property taxes are billed. Even with these changes DOR still has to verify occupancy of applicants. SB157 allowed DOR to define what an applicant can use to determine occupancy in administrative rule. The indicators DOR put in administrative rule are based on the Internal Revenue Service's (IRS) definition of primary residence indicators and include a mailing address for receipt of bills and correspondence; the address on file with the applicant's employer as the place of residence; and the mailing address listed on the applicant's federal and state tax returns, driver's license, car registration, hunting and fishing licenses, or voter registration. These indicators will only be used in cases where DOR staff flag an application for further review.

Starting this year they will pull homeowner information off of the Business and Income Tax Division (BITD) GenTax system and from the Social Security Administration. Gen Tax is BITD's system that houses all income information as reported on individual's income taxes. This will help occupancy verification in that they can check the filing status reported on income taxes within the GenTax system, and flag reports that have an out of state filing status. This along with local staff will help flag instances where they need to gather primary residence indicators from an applicant.

RECOMMENDATION #2

We recommend the Department of Revenue:

- A. Develop and Implement additional management tools to improve income verification between the Property Assessment Division and the Business and Income Tax Division for the Property Tax Assistance Program and the Disabled American Veteran's Exemption, and**
- B. Investigate ways to simplify income documentation provided by applicants for property tax relief programs administered by the department, including the Property Tax Assistance Program and the Disabled American Veteran's Exemption.**

Implementation Status- Implemented

SB157 also changed the application process. Applicants only have to apply once for property tax assistance. After that they remain in the system and are checked for qualification every year based on their income. This check for verification will be done by gathering income information from BITD and the Social Security Administration onto a web application and comparing it to qualification standards for PTAP and DAV. They hope to have this application available by 2017. For this year DOR plans to give applicant information to BITD who will run it through their GenTax system. This query will gather the applicant's income information and assign the proper percent reduction based on that income. If an applicant does not have any income tax information that application will be sent to the Social Security Administration as an additional resource to determine income.

As part of DOR's effort to improve income verification they have added an area in their Orion system where a second social security number can be added to a home owner's record. This assures when they get income information from BITD they will get the entire household income that qualification for assistance is based on. They also have a quality assurance process in place to verify that a homeowner has a social security number attached to their record in the Orion system. If they do not have a social security number attached DOR will send a request for that information to the individual.

SB157 changed the income requirements for PTAP making both PTAP and DAV income requirements based on federally adjusted gross income excluding capital and income losses as calculated on the Montana income tax return for the prior year. For those who don't have to file a Montana income tax return it is based on available income information. This law change made both programs income qualification based on the same information. This along with automatic income verification and a one-time application satisfy part B of the recommendation.

RECOMMENDATION #3

We recommend the Department of Revenue:

- A. Develop and implement a quality control process to improve department efforts to ensure taxpayers applying for the Property Tax Assistance Program or the Disabled American Veteran's Exemption only receive property tax relief on eligible land and improvements, and**
- B. Investigate ways to automate the calculation process within Orion to ensure taxpayers are receiving relief on eligible land and improvements.**

Implementation Status- Implemented

Audit staff was able to review the quality assurance reports that DOR had created to ensure that assistance was only applied to eligible land and improvements. These centered on determining that assistance was not applied to over \$100,000 in taxable market value and 5 acres of land for PTAP. These quality assurance reports became unnecessary with the passage of SB157.

SB157 impacted the eligible land and improvements requirements for PTAP. There are no longer acreage limits that relief can be applied to for PTAP (DAV never had an acreage limit), and it changed the home value that relief can be applied to from \$100,000 in taxable market value to \$200,000 in appraisal value. DAV still has no limit on the home value which relief may be applied to. This has greatly simplified the process of determining what the reduced property tax rate offered by PTAP and DAV will be applied to. With the changes in statute DOR has implemented quality assurance reports that flag any homeowner who is receiving assistance on over \$200,000 in appraisal value. These flagged records are sent to the local offices to determine if this was an error. In some cases the benefit is applied in excess of \$200,000 for an extenuating circumstance, such as a single piece of land with two homeowners who each apply for assistance.

DOR has largely automated the calculation process for PTAP and DAV applicants. Since appraisal value is much simpler to determine than taxable market value DOR's Orion system now automatically applies the reduced tax rate of up to \$200,000 in appraisal value. Based on the income information gathered from BITD's GenTax system DOR has created a program that automatically assigns the proper tax code indicating the individuals benefit. Those tax codes are then assigned to \$200,000 or less in appraisal value automatically in Orion in most cases.

DOR is looking to conduct a mass mailing of the letters that go out to applicants describing the level of assistance, if any, they have been granted. They currently do this after each decision is made individually. A mass mailing will allow them to run quality assurance reports to ensure that assistance has been properly provided before mailing out these letters.

RECOMMENDATION #4

We recommend the department of Revenue:

- A. Develop and implement a quality control process to improve department efforts to ensure taxpayers applying for the Property Tax Assistance Program or the Disabled American Veteran's Exemption receive property tax relief based on their qualifying income; and**
- B. Investigate ways to automate the assignment of tax class codes within Orion to ensure taxpayers are receiving relief based on their qualifying income.**

Implementation Status- Implemented

As described earlier SB157 has changed the income requirements. It changed PTAP income requirements so that both PTAP and DAV are now based on federal adjusted gross income excluding capital and income losses. If the applicant is not required to file an income tax return their social security information is used to determine income. DOR gives their applicant list to BITD who runs it through their Gentax system that contains income reported on Montana state tax returns. Once the income information is pulled out of the Gentax system an automated process is used to assign the proper tax class code that indicates the percent reduction that individual will receive. These applications are separated out by class code and run into the Orion system. The goal moving forward is to eliminate the process of having to run these class code batches into Orion. DOR is developing a web application that will eliminate this step by gathering the information from Gentax and the Social Security Administration and establish the level of benefit before automatically assigning class codes to homeowners all at once. This automated process is the system that is used on about 85 percent of applicants. For 10-15 percent of applicants their benefits must still be hand calculated. These cases involve special circumstances such as half of the property being used as a residence and the other half used for commercial purposes. In these cases the house is taxed at different rates making automatic calculation of benefits impractical. While still developing the final web application the system in place will eliminate human error in most cases, and automate the process.

In eliminating the hand calculation, and hand entering of benefit levels DOR has satisfied the recommendations. They have also implemented a quality assurance process that identifies instances in which the class code does not match the reported income, or the percent reduction assigned to a homeowner.

RECOMMENDATION #5

We recommend the Department of Revenue actively examine their outreach efforts to assess benefit distribution and aid in the administration of property tax relief programs.

Implementation Status – Partially Implemented

DOR staff conducted analysis across the state on owner-occupied homes per PTAP Application. Based on census block groups they also looked at population, median income, and percentage of population below the poverty lines. DOR wanted to look at individual geographic areas across the state, and look at factors outside of the poverty rate that may coincide with more or less usage of PTAP. Going forward they intend to use this analysis to determine how changes in the program such as the one-time application process, and postcard mailings that describe property tax assistance programs to those with qualifying incomes affect usage of the program. DOR also hopes to identify underserved areas. In these cases they can work with local staff to find another way to get higher participation. These are their plans for this information going forward; however, according to staff they have not begun to actively use this information. DOR staff did not provide any analysis conducted for the DAV program.