GOVERNOR'S OFFICE OF
BUDGET AND PROGRAM PLANNING

# Fiscal Note 2025 Biennium

| **Bill information:** | |
|---|---|
| HB0476 - Provide for property tax exemption for certain residential property (Galloway, Steven ) | |
| | |
| **Status:** | As Introduced |

☒Significant Local Gov Impact ☒Needs to be included in HB 2 ☒Technical Concerns

☐Included in the Executive Budget ☒Significant Long-Term Impacts ☐Dedicated Revenue Form Attached

## FISCAL SUMMARY

| | FY 2024 Difference | FY 2025 Difference | FY 2026 Difference | FY 2027 Difference |
|---|---|---|---|---|
| **Expenditures:** | | | | |
| General Fund | $36,000 | $1,154,635 | $225,896 | $987,581 |
| State Special Revenue | $0 | $0 | $0 | $0 |
| **Revenue:** | | | | |
| General Fund | $0 | $0 | ($12,702,000) | ($12,224,000) |
| State Special Revenue | $0 | $0 | ($798,000) | ($768,000) |
| **Net Impact-General Fund Balance:** | ($36,000) | ($1,154,635) | ($12,927,896) | ($13,211,581) |

**Description of fiscal impact:** HB 476 creates a new assessed market value exemption for class 4 residential owner-occupied primary homes. The exemption amount is equal to the appreciation in property value relative to its TY 2023 assessed value. This effectively freezes the market value of eligible property at the TY 2023 (FY 2024) level so long as the property is not sold outside of the immediate family or has improvements made to the property. Reappraisal years coincide with increased exemption amounts due to appreciation in property values. The exempt value decreases revenue for the general fund and the Montana University System. The Department of Revenue (DOR) will require significant FTE in reappraisal years to process exemption applications.

## FISCAL ANALYSIS

**Assumptions:**

**Department of Revenue**

1. Property tax data was analyzed for class 4 residential improvements with unique mailing addresses, excluding multi-family improvements which are not considered eligible for the HB 476 exemption. If a mailing address had more than one property associated with it, the higher value property was assumed to be the primary residence. There are 338,992 class 4 residential improvements with unique mailing addresses in TY 2022.

2. The U.S. Census Bureau 2021 American Community Survey (ACS) estimates there are 311,861 owner-occupied housing units in Montana. It is assumed that the unique mailing address data overstates primary residences by the ratio of the ACS estimate to the DOR property count.
3. There are 378 multi-family improvements with unique mailing addresses, and it is assumed these are primary homes. Subtracting these from the ACS estimate results in an estimate of 311,483 eligible properties.
4. This implies a necessary downward adjustment of 8.11% ((338,992-311,483) / 338,992).
5. The TY 2022 total taxable value of department identified primary homes is $1.549 billion. Based on the HJ 2 growth estimate in class 4 taxable value of 38.11%, that taxable value will be $2.139 billion in TY 2023.
6. Adjusting this value by the overcount of primary homes yields an expected taxable value of primary residences at $1.955 billion.
7. There is an assumed 4% turnover rate of property in the program. This simulates homes either being sold outside of immediate family or significantly improved or added onto.
8. The department reassesses class 4 property values property every two years. Odd years are considered "reappraisal years" and capture changes in value due to appreciation in the fair market price of property. Even years are "off years" where any valuation changes in a property would be due to remodeling or new construction.
9. The exemption provided by HB 476 is first available to properties in TY 2024, which is an off year in the reappraisal cycle. For qualifying owners there is no incentive to apply for an exemption in TY 2024. Any eligible property that applies for and receives the exemption would have no exempt value, since any difference between TY 2023 and TY 2024 values would only be due to activities disqualifying the property from the exemption (see technical note #3).
10. TY 2025 is a reappraisal year, and values will be adjusted to reflect market appreciation. This is the first year that HB 476 has revenue effects. The HJ 2 estimated appreciation in class 4 property is 7.41% in TY 2025. The table below summarizes the fiscal effects in millions of dollars.

| Tax Year | Qualifying Properties | HB 476 Frozen TV (millions) | Current Law TV (millions) | Exempted TV (millions) | General Fund Revenue (millions) | MUS Revenue (millions) |
|---|---|---|---|---|---|---|
| TY 2023 | N/A | $1,955 | $1,955 | $0 | $0 | $0 |
| TY 2024 | 299,000 | $1,877 | $1,877 | $0 | $0 | $0 |
| TY 2025 | 287,100 | $1,802 | $1,935 | $133 | ($12.702) | ($0.798) |
| TY 2026 | 275,600 | $1,730 | $1,858 | $128 | ($12.224) | ($0.768) |

11. The current law TV column is the estimate of the taxable value of qualifying properties if HB 476 did not exist. It is reduced by the assumed yearly 4% attrition rate of property in the program. In reappraisal years it is increased by the growth of class 4 residential property excluding new property and improvements contained in HJ 2.
12. General fund revenue is reduced by the exempted TV multiplied by the 95 mills collected for school equalization plus the weighted half mill (1.5) Vocational Technical School levy in five counties.
13. The Montana University System (MUS) revenue is reduced by the exempted TV multiplied by the 6 mills collected for the university system.
14. Fiscal year is equivalent to the tax year plus one. Therefore TY 2023 corresponds with FY 2024, TY 2024 corresponds with FY 2025, and so on.

*DOR Administrative Costs*

15. The DOR will contract with the software provider for the property tax database to develop and maintain a homestead exemption verification process. Costs associated are roughly $100,000 in FY 2024 for initial setup and then roughly $65,000 annually thereafter.
16. The DOR plans to allow applicants to apply in the second half of the year preceding the tax year that a property owner is claiming an exemption for. For TY 2025, the DOR will begin accepting applications July 1, 2024.

The application period would then run through March 1, 2025. This corresponds with FY 2025, so the fiscal year costs line up with the tax year of the exemption application.

17. There is no reason for homeowners to apply in TY 2024 (see assumption #9). It is assumed applications will be first processed for TY 2025.
18. It is assumed all applications will occur in the reappraisal year, which is FY 2025 and FY 2027.
19. The DOR expects 80% of applications to be submitted online and 20% via paper form. Processing time of paper applications is expected to be about twice as much time as an online submission. The expected number of applications will necessitate 12.00 FTE in FY 2025 and 10.00 FTE in FY 2027.
20. The department will retain 2.00 of these FTE full time for FY 2026 (and beyond) to update records of primary homes that have sold and auditing of the program.
21. Decision letters will be mailed to all applicants. At $0.66 per letter, total costs are expected to be $205,920 in FY 2025, $18,150 in FY 2026, and $169,620 in FY 2027.

| **Fiscal Impact:** | **FY 2024 Difference** | **FY 2025 Difference** | **FY 2026 Difference** | **FY 2027 Difference** |
|---|---|---|---|---|
| **Department of Revenue** | | | | |
| **FTE** | 0.00 | 12.00 | 2.00 | 10.00 |
| **Expenditures:** | | | | |
| Personal Services | $0 | $748,055 | $126,166 | $638,402 |
| Operating Expenses | $36,000 | $406,580 | $99,730 | $349,179 |
| **TOTAL Expenditures** | $36,000 | $1,154,635 | $225,896 | $987,581 |
| **Funding of Expenditures:** | | | | |
| General Fund (01) | $36,000 | $1,154,635 | $225,896 | $987,581 |
| State Special Revenue (02) | $0 | $0 | $0 | $0 |
| **TOTAL Funding of Exp.** | $36,000 | $1,154,635 | $225,896 | $987,581 |
| **Revenues:** | | | | |
| General Fund (01) | $0 | $0 | ($12,702,000) | ($12,224,000) |
| State Special Revenue (02) | $0 | $0 | ($798,000) | ($768,000) |
| **TOTAL Revenues** | $0 | $0 | ($13,500,000) | ($12,992,000) |
| **Net Impact to Fund Balance (Revenue minus Funding of Expenditures):** | | | | |
| General Fund (01) | ($36,000) | ($1,154,635) | ($12,927,896) | ($13,211,581) |
| State Special Revenue (02) | $0 | $0 | ($798,000) | ($768,000) |

**Effect on County or Other Local Revenues or Expenditures:**

1. The average exempted taxable value in TY 2025 and TY 2026 is $131 million. This represents about 2.60% of expected statewide taxable value for those tax years. All else equal, local mills will be on average 2.60% higher in those tax years to offset these tax base reductions.
2. The long-term impacts of HB 476 are larger exemption amounts each reappraisal cycle that cause greater tax shifts. For the TY 2027 and TY 2028 biennium, statewide taxable value will be approximately 5.57% lower and for the TY 2029 and TY 2030 biennium, statewide taxable value will be approximately 7.67% lower. Assuming local mills can float to accommodate this loss in tax base results in similar increases in tax shifts onto other properties.

**Long-Term Impacts:**

1. The exemption granted by HB 476 will grow larger over time, even as the number of properties it applies to gets smaller. The following two biennia are shown in the table below to illustrate this. Each reappraisal year will coincide with an increased exemption granted by HB 476 as home values rise due to market appreciation. Off years of the reappraisal cycle see a decline in the exemption amount as homes fall out of the program due to being sold or significantly improved.

| Tax Year | Qualifying Properties | HB 476 Frozen TV (millions) | Counterfactual TV (millions) | Exempted TV (millions) | General Fund Revenue (millions) | MUS Revenue (millions) |
|---|---|---|---|---|---|---|
| TY 2027 | 264,600 | $1,660 | $1,982 | $321 | ($30.656) | ($1.926) |
| TY 2028 | 254,000 | $1,594 | $1,903 | $309 | ($29.510) | ($1.854) |
| TY 2029 | 243,800 | $1,530 | $2,031 | $501 | ($47.846) | ($3.006) |
| TY 2030 | 234,100 | $1,469 | $1,950 | $481 | ($45.936) | ($2.886) |

**Technical Notes:**

1. A definition of new construction or remodeling is recommended: if any amount of either activity disqualifies a property for the exemption or if some threshold amount must be met. In the absence of a definition, the DOR will need to adopt rules to consider what qualifies.
2. It is likely that the DOR will need rule authority to implement the provisions of HB 476 and the bill should explicitly grant that authority.
3. The exemption created by HB 476 as written is only available to owners of property as of the effective date of the legislation. There is potential for constitutional challenge due to the exemption not being applied uniformly and equitably.

NOT SIGNED BY SPONSOR

| Sponsor's Initials | Date | Budget Director's Initials | Date |
|---|---|---|---|
| | | JW | 2-17-23 |