

PROPERTY ASSESSMENT STUDY COMMITTEE

Study Assignment

A study concerning the impact of the limitation on sales used to value property and the potential impacts if changes are made to the factors used to limit sales to value property. Certain sales are not included in the sales ratio studies to determine assessed valuations based on criteria established by statute. The study shall examine the shifts that may occur from one classification to another, county by county and statewide, if these criteria are amended. The study shall also consider alternative methods used to assess property, including an analysis of methods used by other states.

Summary of Interim

The interim Property Assessment Committee held its first meeting on June 9. Mr. Michael Kenyon, Director of the Division of Property and Special Taxes, and Ms. Colleen Skinner, Department of Revenue and Regulation, explained that it is the director of equalization's responsibility to appraise all property within their jurisdiction at its full and true market value and to treat every property owner equally and fairly under the law.

Mr. Kenyon stated that one of the critical elements in valuing property is sales and when there is a lack of sales, it affects the assessment process. There are three rules enacted by the Legislature that assessors must apply to the assessment process when determining what sales may be used in determining the market:

- 70 acres rule – The 70 acres rule (§ 10-6-33.20) means that the assessor may not use the sale of agricultural land to value other agricultural land if 70 acres of land or less is sold. In 2003, 225 agricultural sales were rejected statewide because of the 70 acres rule, compared to 49 rejections in 1998.
- NA-Z – The NA-Z classification (§ 10-6-33.14) states that if any agricultural land sells for more than 150% of its agricultural income value, the property is classified as NA-Z and is taxed for one year at the value the property was sold. The following year the property is classified and assessed according to its current use. The NA-Z sales are not used for market comparisons. In 2003, 696 agricultural sales were rejected statewide because of the NA-Z rule, compared to 319 rejections in 1998.
- 150% rule – The 150% rule (§ 10-6-74) throws out both agricultural and non-agricultural sales when property sells for more than 150% of its assessed value. The assessor may not use these sales for market comparisons. In 2003, 287 agricultural sales were rejected pursuant to this rule, compared to 2 in 1998. There were 2,469 non-agricultural sales rejected in 2003, compared to 27 in 1998.

Mr. Kenyon stated that number of sales available to use in the assessment process continues to decrease. In 2003, fifty-one of the sixty-six counties had less than ten usable agricultural sales per county. Another factor limiting the number of usable sales is that seventy-five percent of the statewide sales are not-arms-length transactions and are not used for assessing property. The assessor has to have at least fifteen usable sales over a three year period to establish the market for agricultural land. If a county does not have fifteen usable sales, then the assessor may bridge to other counties or use the agricultural income approach as provided in § 10-6-33.24.

Mr. Deene Dayton, Legislative Audit, also spoke to the committee and distributed a handout entitled "Property Tax Limitations" and explained that the tax limitation impacts the property tax levy in dollars, not the local government's budget. The impact of the tax limitation varies for each entity because the portion of the budget financed by property taxes varies from local government to local government.

The interim committee focused attention at the August 16 and 17 meeting on the science and practice of assessing real property as explained by several experts in the field. The committee also reviewed alternative methodologies for arriving at property values that are used in other states. It was also explained that there are no property tax breaks, but only tax shifts.

In discussing the effects of the 150% throw-out rules for sales of real property, the Revenue Department presented statistical information which disclosed a disparity in some counties between the levels of assessment of agricultural property compared to non-agricultural property. This throw-out rule creates significant disparities between some counties, meaning that property owners across the state are not always treated equally. However, the disparities do not always favor agricultural property. The exclusion of certain sales because of the 150% rules means some counties appear poorer than they really are for purposes of the school funding formula.

Members received a briefing on the use of rental income to value agricultural property. Following that briefing was a discussion concerning the most effective method to acquire valid rental income data and to determine a fair capitalization rate when computing accurate values. There was testimony indicating that the sales prices of property were rising faster than rental rates because land is now seen as an attractive investment opportunity. Arguably, this means that land valued through a method based upon rental information would more closely approximate the productive value of land. Members also heard testimony regarding the 7.75 percent cap rate and the use of soil surveys in determining how properties are valued when the income approach is used. Concern was expressed that the effective cap rate is too high and does not reflect the market value of land. Interested parties also testified that reliance on the soil survey is too extensive under the income approach and that other factors including topography, obstructions (primarily rocks) and rainfall must be given greater weight.

The directors of equalization were actively involved in the interim by making presentations, responding to committee questions, and commenting on draft legislation. The directors provided information on the concerns with the factors limiting sales, their experiences, and current trends.

The third meeting of this study committee was held on September 13 and 14 and was devoted to the review of proposed legislation concerning property tax classifications and the factors and methods used to assess property.

The committee reviewed fifteen legislative proposals and approved eight.

Listing of Legislation Adopted

1. *An Act to revise the requirements for determining whether dwellings are eligible to be classified as owner-occupied single-family dwellings.* The legislation clarifies that each married couple may only claim one home as owner-occupied and that a home must be the owner's principal place of residence.

2. *An Act to establish certain presumptions concerning real property sales used to value property.* That all sales of property are presumed to be arm-length transactions until documented otherwise.
3. *An Act to revise the procedure for assessing agricultural property and to repeal certain factors used to determine which sales may be used in assessing property.* The proposed legislation mandates the use of production income as the means to value agricultural income property and repeals the 70 acres and 150 percent rules and the NA-Z classification.
4. *An Act to require written statements to be filed concerning the leasing of agricultural land and to establish certain penalties.* The lessor or lessee of agricultural property would be required to file a statement outlining the lease payments and relevant provisions of any rental agreement related to agricultural property.
5. *An Act to permit adjustment for certain factors that may affect the agricultural income value of land.* When land is valued pursuant to the agricultural income approach, this proposal will permit the director of equalization to make adjustments for factors other than soil type.
6. *An Act to revise the method used to determine the capacity of land to produce agricultural products.* The director shall consider whether the land is tillable or nontillable when determining the capacity of land to produce.
7. *An Act to establish additional classifications for agricultural property.* The proposal creates subclasses of agricultural land based on the land meeting certain factors or being used for certain purposes.
8. *An Act to revise certain provisions concerning the determination of agricultural income values for classifying nonagricultural acreages.* Revise certain provisions concerning the NA-Z classification to correspond with the terminology used to determine agricultural income value.

Summary of Meeting Dates & Places and Listing of Committee Members

The committee met on June 9, August 16 and 17, and September 13 and 14. The committee meetings were located in Pierre.

Committee members were: Senator Dave Knudson, Chair; Representative Larry Rhoden, Vice-Chair; Senators Tom Dempster, Brock Greenfield, Frank Kloucek, Paul Symens, and Drue Vitter; and Representatives Daryl Christensen, Thomas Dadrack, Art Fryslie, Dale Hargens, Jim Hundstad, Jim Lintz, Casey Murschel, Jim Peterson, Lou Sebert, and Keri Weems.

Staff members were: Fred Baatz, Principal Research Analyst; Jim Fry, Director; and Kris Schneider, Legislative Secretary.