

SUBJECT: Limiting property tax appraisals and making senior tax exemptions portable

COMMITTEE: Select Committee on Revenue and Public Education Funding — committee substitute recommended

VOTE: 7 ayes — Sadler, Hilbert, Brimer, Chisum, Hochberg, Williamson, Wilson
0 nays
4 absent — Craddick, Hernandez, Junell, Stiles

SENATE VOTE: On final passage, April 22 — 30-0

WITNESSES: For — Wendell Wesklake, Texas Taxpayers and Research Association; Buddy Winn, Brazos County Tax Assessor
Against — John Lewis, Travis County Taxpayers Coalition
On — Sheryl N. Cole, Texas Municipal League; Kathryn Heidemann, Williamson County Taxpayers; Richard Lavine, Center for Public Policy Priorities; Fred K. Paine, Concerned United Taxpayers; Jim Robinson, Harris County Chief Appraiser; Gwen Selby

BACKGROUND : For an overview of property tax appraisal issues, see *The Tax System and Public School Financing in Texas*, House Research Organization Session Focus Report Number 75-11, March 24, 1997.

DIGEST: CSSB 841 would limit increases in appraised property values, restrict the frequency of appraisals, increase the capability of appraisal districts to hear taxpayer protests, and establish a new state level administrative review process for protesting appraisals in cases valued at \$1 million or more.
The bill also would allow seniors to transfer their property tax freezes and provide nonprofit organizations a 60-day period to remedy any deficiency in applying for tax exemptions.

Homestead appraisals. CSSB 841 would limit the appraised value of a homestead to the market value of the property or to 105 percent of the appraised value of the property for the preceding year, plus new improvements, whichever was less. The appraiser would have to record both the market value and the 105 percent value. The limitation would take effect the second year a person owned the homestead property and would expire January 1 of the first tax year that the property owner or spouse, surviving spouse, or minor child qualified for the homestead exemption.

Persons could abate or defer a suit to collect delinquent taxes on the portion of the appraised value of their homestead that exceeded the 105 percent benchmark. The abatement or deferral would not apply if taxes were delinquent on the 100 percent appraised value of the homestead. The bill would provide the procedures to be used to obtain a deferral or abatement. Upon finding that the individual was entitled to the deferral, a court would have to abate the suit until the property was no longer the person's homestead. The deferral or abatement would only apply to taxes due the second year the person owned the homestead. The tax lien would remain on the property and the interest would accrue at 8 percent annual interest during the deferral period; however, no penalty could be assessed during the deferral period.

The bill would limit the frequency of appraisals on a homestead to no more than once every three years, unless property improvements increased the value of the house by at least 10 percent before the third year.

Methods of appraising property. The bill would require that property be appraised by generally accepted appraisal methods and techniques, including mass appraisal standards recognized by the Uniform Standards of Professional Appraisal Practice.

The bill would specify the requirements for using different methods of appraising property:

- **Cost method** — The chief appraiser would have to use cost data obtained from accepted sources, to make adjustments for physical, functional or economic obsolescence, and to make all applicable market data available on upon request.

- **Income method** — The appraiser would have to use rental income, projections of future rental incomes only based on clear evidence, and the capitalization rate for income-producing property.
- **Market data comparison** — The appraiser would use comparable sales data, if possible, in determining the market value of real property.

The bill would specify alternative methods of calculating appraisal of oil and gas producing property and require the chief appraiser to use the method requested by the property owner if it would result in an accurate calculation of the market value of the property. The requested methods could include a discounted cash-flow analysis and a gross-income multiplier. Chief appraisers would have to notify owners if they determined that the method requested would not accurately calculate the property value. The determination could be appealed to the appraisal review board for a final determination on how the property should be valued.

The bill would prohibit land from being designated as open-space land for valuation purposes if a contiguous parcel of the land was not eligible for the open-space valuation. The denial of open-space valuation would not apply if a parcel of the land was a person's homestead.

Appraisal notification and protests. The appraisal notification from the chief appraiser would have to include the taxable value of the property and provide a detailed explanation of the time and procedure for protesting the valuation. The bill would repeal the simplified tax rate notice for small taxing units.

If the determination was protested, the appraisal district would have the burden of proving the value of the property by a preponderance of the evidence. If the district failed to meet that standard, the protest would have to be determined in favor of the property owner. When the protest claimed unequal appraisal of property, the appraisal district would have to prove that the property value was not greater than the median level sampled of other like properties.

An appraisal review board would be required to hold a weekend or evening hearing if requested by the property owner.

The bill would require the State Office of Administrative Hearings (SOAH) to hear property protest cases valued at \$1 million or more. Property owners would be required to file a \$100 filing fee and would forfeit the right to have a hearing before their appraisal review board. The final ruling of the SOAH administrative law judge would be binding on all parties. The appraisal district would be required to reimburse the SOAH for the costs of the property tax hearing.

Appraisal boards. CSSB 841 would increase each appraisal district governing board to six members: five appointed by participating taxing units plus the county assessor-collector as an ex-officio member and board chair.

The bill would increase the number of auxiliary members appointed by the board of directors of an appraisal district to hear taxpayer protests and to assist the board:

- in counties with populations of 1 million or more, the number would increase from 30 to 66;
- in counties of 500,000 to 1 million, from 20 to 45;
- in counties of 250,000 to 500,000, from 10 to 25; and
- in counties of less than 250,000, from 6 to 10.

Property tax exemptions. The bill would allow property tax freezes for persons 65 and over to be transferred to a different homestead in the same proportion as the previous homestead. If the qualifying senior died, the freeze would transfer to a spouse aged 55 years of age or older so long as the surviving spouse continued to live in the home.

A person receiving a disabled or an elderly residence exemption could not receive one of these exemptions on more than one residence homestead in the same year.

Persons qualifying for a 65 or over exemption would be required to notify the chief appraiser of their qualifications before their 66th birthday.

The bill would require that property taxes be allocated according to the type of appraisal valuation that each owner was entitled to when they owned the

property. It would impose a penalty of 50 percent on delinquent taxes due when the chief appraiser cancelled a homestead exemption because: the property was not the person's principal residence, the person had received a homestead exemption on another property, the person was younger than 65 but receiving an exemption for those 65 and over, or the qualifying senior died and the spouse was younger than 55. The 50 percent penalty would not apply if the property owner notified the chief appraiser of the disqualifying circumstances.

The bill would specify identifying information to be included on the application forms for property tax exemptions and for homestead exemptions, and would apportion property tax exemptions for residential homesteads to each owner based on the percentage of ownership in the property.

Charitable, youth, religious, and educational organizations qualifying for a property tax exemption would have to use their assets in performing the organization's official function instead of merely pledging their assets. The bill would specify that religious or youth development organizations and schools be organized and operated primarily for their state purpose.

The bill would allow nonprofits to transfer their assets to the federal government upon their dissolution and would specify that compliance with provisions of a contract with the federal government would not affect the nonprofit's eligibility for property tax exemption.

If a chief appraiser determined that a nonprofit's property tax exemption application was invalid due to certain deficiencies in documentation, the appraiser would have to allow the organization 60 days to remedy the deficiency. Once the deficiency was remedied, the organization would be eligible for the tax exemption.

Effective date. CSSB 841 would take effect only if HJR 4 was not approved by the voters and SJR 43 was approved by the voters in November 1997.

SUPPORTERS
SAY:

CSSB 841 is a compilation of the property tax provisions the House debated and passed in HB 4 earlier in the session. It would tighten up the application process for 65 and over exemptions to prevent “double dipping” and to ensure that persons entitled to the exemption received them. Also, it would provide stiff penalties for those individuals receiving property tax exemptions to which they were not entitled. It would strengthen and clarify the rights of property owners regarding appraisals and valuations and limit the amount and frequency of homestead appraisals.

Persons age 65 and older who currently enjoy a freeze on their school taxes should not lose their tax break if they choose to move. Current law penalizes persons 65 and over who move to a different residence even though many people in this age category often move to smaller homes because they need less space. Some are also forced to move because they cannot afford to pay other property taxes assessed on their current home. However, by moving, they lose the school tax freeze that they enjoyed.

The tax freeze for seniors is a benefit that should follow individuals, not the property they happened to be living in at the time they turned 65. Senior citizens should not be forced to stay in the same home after they turn 65 just to retain their property tax freeze.

The bill would give oil and gas property owners other methods to appraise their property so long as it did not lower the valuations. It would also give industrial and commercial property owners the option to have appraisal protest cases handled by SOAH instead of appealing to the appraisal board; SOAH would be more objective in the assessment of the situation.

Requiring that the tax assessor-collector, an elected official, chair the appraisal board would make boards more responsive and accountable to the people.

The bill also would put a stop to the current practice of reappraising homes every year, with no limit on the increase in appraisal values. This can be particularly onerous for homeowners in fast-growth areas who have seen huge increases in their appraised property value each year, greatly adding to their property tax burden. The bill would limit the number of times that a home could be reappraised to no more than once every three years and limit

the annual percentage increase to 5 percent a year, which would assure homeowners that their property value could not go higher than 15 percent every three years. This reasonable limit would allow higher property valuations to be phased in over time and add some needed predictability to the system.

Property taxes in Texas are too high, as evidenced by the governor's initiative to lower school property taxes. To provide needed relief, tax rates could be limited or capped, but this would not prevent "tax creep" as the total tax bill for many homeowners continues to soar due to sharp hikes in their appraised valuation.

CSSB 841 also would prohibit industry from taking advantage of open-space land designations to lower their property tax liability. The provision would close a loophole now being used by some business interests. For example, under CSSB 841 power companies could no longer put a few cows to graze under power lines, have the land designated open-space land, and pay lower taxes.

The bill would correct a technical difficulty in the Tax Code that could prevent some nonprofit churches and other religious organizations from receiving property tax exemptions. The Tax Code requires that, to qualify for tax exemption, an organization has to pledge its assets for use in performing its charitable functions. Though nonprofits' assets are by definition pledged to performing such functions, their charters may not expressly state this pledge. This has endangered the tax exempt status of certain organizations that, although in spirit meet all requirements for tax exemption, could be interpreted as violating the law.

In addition, many nonprofit organizations receive some federal funds, which are required by federal law to be returned to Washington upon the organization's dissolution. State law requires, however, that tax-exempt nonprofits return assets to the state or to a similar nonprofit upon dissolution. The bill would allow nonprofits to adhere to federal law and still receive a property tax exemption.

The Tax Code has become so intricate and cumbersome that in order to comply with its provisions, many nonprofits must hire lawyers and tax

consultants. Many churches and small nonprofits, however, cannot afford such professional assistance. Texas' tax law should not be so complicated that even when they try, law-abiding individuals are unable to comply. For this reason, the bill would allow certain nonprofits extra opportunity to remedy any paperwork irregularities that might jeopardize their tax exemptions. The bill would simplify the Tax Code and ensure all Texas' many worthy nonprofits equal treatment under the law.

OPPONENTS
SAY:

The bill's provisions would cost the general revenue fund a total of nearly \$200 million between 2000 and 2002 alone to make the for lost school revenues at the local level. These costs would continue to increase each year thereafter.

Allowing commercial and industrial property owners and wealthy people with properties worth more than \$1 million to appeal their valuation cases to the SOAH would not be equal treatment of taxpayers.

County tax assessor-collectors generally do not know much about the tax appraisal process. Placing them on the board is one thing, but having someone unfamiliar with appraisal business and whose main job is collecting taxes would not make boards more efficient.

The language regarding designation of open-space land is ambiguous and could lead to differing interpretations by tax appraisers. As a result, a person who leased a contiguous piece of property that was used for commercial purposes could jeopardize the open-space valuation designation.

This bill would cap the appraisal valuations on homesteads and allow them to be treated differently than commercial or industrial property. This would be blatantly unfair by causing non-residential property to bear the costs of limitation on homestead valuations. If local governments are forced to raise tax rates to compensate for an artificial limit on appraised values, everyone could end up paying more, especially non-residential property owners.

Capping the percentage valuation increase for homesteads and limiting the frequency of appraisals could be a two-edge sword. Although it could help homeowners in fast growing areas that are experiencing large annual

increases in property values, it could hurt those very same people when growth slows. If homestead property can only be reappraised every three years and value increases capped at 5 percent a year, then appraisal districts might be inclined to automatically raise appraisals 15 percent every three years because it would be another three years before they could change the appraised value.

The three-year appraisal lag could actually backfire on homeowners. Three years could be a long time between appraisals, especially since market values could go down. The overall effect could be to cause tax rates to skyrocket to make up the needed tax dollars.

Instead of capping appraisal values and limiting frequency of appraisals, which would artificially skew property values and result in unequal taxation, it would be better to lower the tax rates for homeowners. Under the House version of HB 4, residential property taxes for public school maintenance and operation would drop from \$1.30 per \$100 valuation to 64 cents and the Senate version would lower the tax rate by 17 cents.

The portability of the 65 and over school tax freeze should be carefully structured to provide relief only to those seniors who actually need the exemption. One option would be to weight the amount of the exemption that was transferable based on the income of the individual. Other proposals would allow the freeze to be transferred only if the person was forced to move because of governmental action, such as condemnation of the property.

The property tax losses to school districts caused by this provision would be costly to the state because general revenue would have to make up the shortfall in local funds caused by portability of the tax freeze. The fiscal note to SJR 43 indicates that it would cost the state more than \$25 million by fiscal 2002, and this figure would increase each year thereafter.

NOTES:

The Senate-passed version of SB 841 addressed appraisal boards, number of auxiliary members, duplication of homestead exemptions, homestead exemption application forms, appraisal methods, and deferred property taxes on appreciating homesteads.

SJR 43 by Cain, the constitutional amendment to limit maximum annual increases in homestead appraisal valuations and allow portability of the senior tax freeze, was adopted by the House on May 22.

HJR 4, the constitutional amendment required for the comprehensive tax bill, is in conference committee.