Approved: 3-31-95

Date

MINUTES OF THE HOUSE COMMITTEE ON TAXATION.

The meeting was called to order by Chairperson Phill Kline at 9:00 a.m. on March 9, 1995 in Room 519-S of the Capitol.

All members were present except: Rep. Phil Kline - excused
Rep. Doug Lawrence - excused
Rep. Jack Wempe - excused

Committee staff present: Chris Courtwright, Legislative Research Department
Tom Severn, Legislative Research Department
Don Hayward, Revisor of Statutes
Ann McMorris, Committee Secretary

Conferees appearing before the committee: listed after each bill heard.

Others attending: See attached list

In the absence of Chair Kline, Vice Chair Hayzlett presided.

Chair Hayzlett opened the hearing on:

SB 41 - Interest on refunds of protested property taxes

Proponents:
Shelby Smith, Rural Kansas Taxpayers Association, Wichita (Attachment 1)
Bernard Hentzen, Hentzen Consulting Service, Wichita

Mr. Hentzen indicated he favored the proposal to pay interest to the taxpayers who have been forced to pay taxes that have been improperly applied. At the close of his testimony, Mr. Hentzen asked permission to return to the podium after the opponents had been heard. Vice Chair acknowledged his request but didn't indicate what action he would take.

Senator Don Sallee

Senator Sallee urged passage of this bill as it gives the taxpayer an opportunity early in the year to appeal their taxes before time to pay them. Currently the county does collect interest on overpaid tax money while it is being appealed and this interest is not returned to the taxpayer.

Opponents:
Willie Martin, Sedgwick County (Attachment 2)
Ann Spiess, Kansas Association of Counties

Ms. Spiess indicated she supported either of the two amendments submitted in the testimony of Willie Martin.

Vice Chair in response to Mr. Hentzen's request to rebuttal said he had conferred with the ranking minority member and another member and noted it was not proper procedure to permit further comments.

Vice Chair closed the hearing on **SB 41**.

MINUTES OF THE HOUSE COMMITTEE ON TAXATION, Room 519-S Statehouse, at 9:00 a.m. on March 9, 1995.

Chair opened hearing on:

SB 165 - Redemption of real property subject to sale for delinquent taxes

Proponent:
Gerry Ray, City of Overland Park, Johnson County Board of Commissioners (Attachment 3)

Chair closed hearing on **SB 165**

Rep. Donovan wished to go on record as objecting to Chair not allowing rebuttal by proponent to the opponents' amendments on **SB 41** on the grounds that he had withheld questions during the testimony awaiting the further comments of Mr. Hentzen. Vice Chair responded he did not agree to let Mr. Hentzen return but had acknowledged his request pending an opportunity to check proper procedure and had determined this to be inappropriate action.

Chair opened hearing on :

SB 275 - Fair market value for property tax purposes, considerations in determining.

Proponents:
Janet Stubbs, Kansas Building Industry Association (Attachment 4)
Gordon Garrett, Commercial Property Association of Kansas (Attachment 5)

Richard Rodewald
Suggested the word "absorption" be changed to "inventory sellout life" or "inventory completion life"

Chair closed hearing on **SB 275.**

Adjournment.

The next meeting is scheduled for March 10, 1995.

TAXATION COMMITTEE GUEST LIST

DATE: MARCH 9- 1995

NAME	REPRESENTING
SHELBY Smith	KCTA
RICHARD RODEWALD	TAXPAYERS
ART BROWN	MID-AM LUMBER
JANET STUBBS	KBIA
Gordon T. Garrett	CPAK
Trudy Perkins	CPAK
Shannon Peterson	KBA
Gerry Ray	Johnson Co Comm
M. Martin	Sedgwick Co.

THE SHELBY SMITH group

TESTIMONY
Senate Bill No. 41
Payment of Interest on Refunds of Protested Real Estate Taxes
March 9, 1995

Mr. Chairman and Members, House Assessment and Taxation Committee

I'm appearing here today on behalf of the Rural Kansas Taxpayer's Association (RKTA) the original supporter of SB 41.

RKTA is not a tax protest group, but rather a tax equity association of about 500 farmers and agricultural business taxpayers. We were organized in 1994 by Mr. Larry Peterson, President, Property Tax Services, Inc., a tax consultant who has specialized in grain elevator and commercial property valuations since 1989.

Current law and practice is to charge interest on overdue and underpayment of taxes, and then not rebate with interest on illegal and over-payment of taxes. This is grossly unfair and unjust. IT IS ABUSE OF POWER.

Additionally, this creates a disincentive in the appeal process. It's in the County's best interest to invest the money and not refund in a timely manner. What's good for the goose is good for the gander, SB 41 provides:

- An interest rate of 12% per annum which is the same rate charged delinquent taxpayers. A precedent 12% rate, I believe can also be found in the Kansas Income Tax code.
- Interest is computed from the date the taxes are paid or when due, whichever is later.
- 30 day time limit for the County Treasurer to refund the protested taxes and interest upon receipt of the refund order or change by the County Appraiser following the protest hearing.

We also recommend that the reimbursed interest be charged to the County General Fund (CGF). Delinquent interest received is credited to the CGF (KSA 79-2004).

This bill is good public policy. IT IS A BILL WHOSE TIME HAS COME!

Respectfully,

Shelby Smith - Lobbyist, RKTA

House Taxation
3-9-95
Attachment 1

132 South Fountain
Wichita, Kansas 67218
316-684-1371

820 S.E. Quincy, Suite 312
Topeka, Kansas 66612
913-235-9034

PUBLIC AFFAIRS CONSULTANTS

SEDGWICK COUNTY, KANSAS

INTERGOVERNMENTAL RELATIONS

WILLIE MARTIN

COUNTY COURTHOUSE• 525 N. MAIN• SUITE 315• WICHITA, KANSAS 67203• TELEPHONE (316)383-7552

TO: HOUSE COMMITTEE ON TAXATION
FROM: WILLIE MARTIN
SUBJ.: SENATE BILL 41
DATE: MARCH 9, 1995

Mr. Chairman and members of the Committee, thank you for the opportunity to express our concerns about Senate Bill 41. I am Willie Martin, and I represent the Sedgwick County Board of Commissioners.

We understand the need to make timely and equitable refunds to taxpayers. However, we believe requiring counties to pay interest for the period of time appeals are with BOTA is inequitable to all Sedgwick County taxpayers. Counties are responsible for the appeals process at the local level. We have no control over the process for appeals made to BOTA.

We respectfully submit two amendments for your consideration.

The first, would require the county to pay interest from the date taxes were paid or required to be paid, whichever is later, until the date the appeal was filed with the state board of tax appeals.

The second, would assess interest when the board of tax appeals or a court of competent jurisdiction has specifically found that the county's position has no basis in fact or in law and is frivolous.

Sedgwick County hopes you will use one of these as an amendment to Senate Bill 41. We believe such action would make the bill fair and equitable to both the taxpayer and counties.

Thank you for your consideration of our concerns.

House Taxation
3-9-95
Attachment 2-1

Sedgwick County's first amendment to:

SENATE BILL NO. 41

By Committee on Assessment and Taxation

1-12

AN ACT relating to property taxation; providing for payment of interest on refunds of protested taxes; amending K.S.A. 1994 Supp. 79-2005 and repealing the existing section.

Be it enacted by the legislature of the State of Kansas:

Section 1. K.S.A. 1994 Supp. 79-2005 is hereby amended to read as follows: 79-2005. (a) Any taxpayer, before protesting the payment of such taxpayer's taxes, shall be required, either at the time of paying such taxes, or, if the whole or part of the taxes are paid prior to December 20, no later than December 20, or, with respect to taxes paid in whole on or before December 20 by an escrow or tax service agent, no later than January 31 of the next year, to file a written statement with the county treasurer, on forms approved by the state board of tax appeals and provided by the county treasurer, clearly stating the grounds on which the whole or any part of such taxes are protested and citing any law, statute or facts on which such taxpayer relies in protesting the whole or any part of such taxes. When the ground of such protest is that the valuation or assessment of the property upon which the taxes are levied is illegal or void, the county treasurer shall forward a copy of the written statement of protest to the county appraiser who shall within 15 days of the receipt thereof, schedule an informal meeting with the taxpayer or such taxpayer's agent or attorney with reference to the property in question. the county appraiser shall review the appraisal of the taxpayer's property with the taxpayer or such taxpayer's agent or attorney and may change the valuation of the taxpayer's property, if in the county appraiser's opinion a change in the valuation of the taxpayer's property is required to assure that the taxpayer's property is valued according to law, and shall, within 15 business days thereof, notify the taxpayer in the event the valuation of the taxpayer's property is changed, in writing of the results of the meeting. In the event the valuation of the taxpayer's property is changed and such change requires a refund of taxes, the county treasurer shall process the refund in the manner provided by subsection (l).

(b) No protest appealing the valuation or assessment of property shall be filed pertaining to any year's valuation or assessment when an appeal of such valuation or assessment was commenced pursuant to K.S.A. 79-1448, and amendments thereto, nor shall the second half payment of taxes be protested when the first half payment of taxes has been protested. Notwithstanding the foregoing, this provision shall not prevent any subsequent owner from protesting taxes levied

2-2

for the year in which such property was acquired, nor shall it prevent any taxpayer from protesting taxes when the valuation or assessment of such taxpayer's property has been changed pursuant to an order of the director of property valuation.

(c) A protest shall not be necessary to protect the right to a refund of taxes in the event a refund is required because the final resolution of an appeal commenced pursuant to K.S.A. 79-1448, and amendments thereto, occurs after the final date prescribed for the protest of taxes.

(d) If the grounds of such protest shall be that the valuation or assessment of the property upon which the taxes so protested are levied is illegal or void, such statement shall further sate the exact amount of valuation or assessment which the taxpayer admits to be valid and the exact portion of such taxes which is being protested.

(e) If the grounds of such protest shall be that any tax levy, or any part thereof, is illegal, such statement shall further state the exact portion of such tax which is being protested.

(f) Upon the filing of a written statement of protest, the grounds of which shall be that any tax levied, or any part thereof, is illegal, the county treasurer shall mail a copy of such written statement of protest to the state board of tax appeals and the governing body of the taxing district making the levy being protested.

(g) Within 30 days after notification of the results of the informal meeting with the county appraiser pursuant to subsection (a), the protesting taxpayer may, if aggrieved by the results of the informal meeting with the county appraiser, appeal such results to the state board of tax appeals.

(h) After examination of the copy of the written statement of protest and a copy of the written notification of the results of the informal meeting with the county appraiser in cases where the grounds of such protest is that the valuation or assessment of the property upon which the taxes are levied is illegal or void, the board shall conduct a hearing in accordance with the provisions of the Kansas administrative procedure act, unless waived by the interested parties in writing. If the grounds of such protest is that the valuation or assessment of the property is illegal or void the board shall notify the county appraiser thereof.

(i) In the event of a hearing, the same shall be originally set not later than 90 days after the filing of the copy of the written statement of protest and a copy, when applicable, of the written notification of the results of the informal meeting with the county appraiser with the board. In all instances where the board sets a request for hearing and requires the representation of the county by its attorney or counselor at such hearing, the county shall be represented by its county attorney or counselor.

(j) When a determination is made as to the merits of the tax protest, the board shall render and serve its order thereon. The county treasurer shall notify all affected taxing districts of the amount by which tax revenues will be reduced as a result of a refund.

(k) If a protesting taxpayer fails to file a copy of the written statement of protest and a copy, when applicable, of the written notification of the results of the informal meeting with the county

appraiser with the board within the time limit prescribed, such protest shall become null and void and of no effect whatsoever.

(l) In the event the board or a *court of competent jurisdiction* orders that a refund be made and no appeal is taken from such order, *or in the event of a change in valuation which results in a refund pursuant to subsection (a)*, the county treasurer shall, ~~as soon thereafter as reasonably practicable~~ *within 30 days after such order or change becomes final,* ~~refund to the taxpayer such protested taxes from tax moneys collected but not distributed. If the county treasurer fails to~~ *refund such protested taxes* ~~within 30 days, such protested taxes~~ *plus interest at the rate of 12% per annum from the date such taxes were paid or required to be paid, whichever is later,* until the date the appeal was filed with the state board of tax appeals ~~shall be refunded~~ *to the taxpayer from tax monies collected but not distributed.* Upon making any such refund, the county treasurer shall charge the fund or funds having received such protested taxes **except that, with respect to that portion of any such refund attributable to interest, the county treasurer shall charge the county general fund.**

(m) Whenever, by reason of the refund of taxes previously received or the reduction of taxes levied but not received as a result of decreases in assessed valuation, it will be impossible to pay for imperative functions for the current budget year, the governing body of the taxing district affected may issue no-fund warrants in the amount necessary. Such warrants shall conform to the requirements prescribed by K.S.A. 79-2940, and amendments thereto, except they shall not bear the notation required by such section any may be issued without the approval of the state board of tax appeals. The governing body of such taxing district shall make a tax levy at the time fixed for the certification of tax levies to the county clerk next following the issuance of such warrants sufficient to pay such warrants and the interest thereon. All such tax levies shall be in addition to all other levies authorized by law.

(n) The county treasurer shall disburse to the proper funds all portions of taxes paid under protest and shall maintain a record of all portions of such taxes which are so protested and shill notify the governing body of the taxing district levying such taxes thereof and the director of accounts and reports if any tax protested was levied by the state.

(o) This statute shall not apply to the valuation and assessment of property assessed by the director of property valuation and it shall not be necessary of any owner of state assessed property, who has an appeal pending before the board of tax appeals, to protest the payment of taxes under this statute solely for the purpose of protecting the right to a refund of taxes paid under protest should that owner be successful in that appeal.

Sec. 2. K.S.A. 1994 Supp. 79-2005 is hereby repealed.

Sec. 3. This act shall take effect and be in force from and after its publication in the statute book.

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Sedgwick County's second amendment to:

SENATE BILL NO. 41

By Committee on Assessment and Taxation

1-12

AN ACT relating to property taxation; providing for payment of interest on refunds of protested taxes; amending K.S.A. 1994 Supp. 79-2005 and repealing the existing section.

Be it enacted by the Legislature of the State of Kansas:

Section 1. K.S.A. 1994 Supp. 79-2005 is hereby amended to read as follows: 79-2005. (a) Any taxpayer, before protesting the payment of such taxpayer's taxes, shall be required, either at the time of paying such taxes, or, if the whole or part of the taxes are paid prior to December 20, no later than December 20, or, with respect to taxes paid in whole on or before December 20 by an escrow or tax service agent, no later than January 31 of the next year, to file a written statement with the county treasurer, on forms approved by the state board of tax appeals and provided by the county treasurer, clearly stating the grounds on which the whole or any part of such taxes are protested and citing any law, statute or facts on which such taxpayer relies in protesting the whole or any part of such taxes. When the grounds of such protest is that the valuation or assessment of the property upon which the taxes are levied is illegal or void, the county treasurer shall forward a copy of the written statement of protest to the county appraiser who shall within 15 days of the receipt thereof, schedule an informal meeting with the taxpayer or such taxpayer's agent or attorney with reference to the property in question. The county appraiser shall review the appraisal of the taxpayer's property with the taxpayer or such taxpayer's agent or attorney and may change the valuation of the taxpayer's property, if in the county appraiser's opinion a change in the valuation of the taxpayer's property is required to assure that the taxpayer's property is valued according to law, and shall, within 15 business days thereof, notify the taxpayer in the event the valuation of the taxpayer's property is changed, in writing of the results of the meeting. In the event the valuation of the taxpayer's property is changed and such change requires a refund of taxes, the county treasurer shall process the refund in the manner provided by subsection (l).

(b) No protest appealing the valuation or assessment of property shall be filed pertaining to any year's valuation or assessment when an appeal of such valuation or assessment was commenced pursuant to K.S.A. 79-1448, and amendments thereto, nor shall the second half payment of taxes be protested when the first half payment of taxes has been protested. Notwithstanding the foregoing, this provision shall not prevent any subsequent owner from protesting taxes levied for the year in which such property was acquired, nor shall it prevent any taxpayer from protesting taxes when the valuation or assessment of such taxpayer's

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property has been changed pursuant to an order of the director of property valuation.

(c) A protest shall not be necessary to protect the right to a refund of taxes in the event a refund is required because the final resolution of an appeal commenced pursuant to K.S.A. 79-1448, and amendments thereto, occurs after the final date prescribed for the protest of taxes.

(d) If the grounds of such protest shall be that the valuation or assessment of the property upon which the taxes so protested are levied is illegal or void, such statement shall further sate the exact amount of valuation or assessment which the taxpayer admits to be valid and the exact portion of such taxes which is being protested.

(e) If the grounds of such protest shall be that any tax levy, or any part thereof, is illegal, such statement shall further state the exact portion of such tax which is being protested.

(f) Upon the filing of a written statement of protest, the grounds of which shall be that any tax levied, or any part thereof, is illegal, the county treasurer shall mail a copy of such written statement of protest to the state board of tax appeals and the governing body of the taxing district making the levy being protested.

(g) Within 30 days after notification of the results of the informal meeting with the county appraiser pursuant to subsection (a), the protesting taxpayer may, if aggrieved by the results of the informal meeting with the county appraiser, appeal such results to the state board of tax appeals.

(h) After examination of the copy of the written statement of protest and a copy of the written notification of the results of the informal meeting with the county appraiser in cases where the grounds of such protest is that the valuation or assessment of the property upon which the taxes are levied is illegal or void, the board shall conduct a hearing in accordance with the provisions of the Kansas administrative procedure act, unless waived by the interested parties in writing. If the grounds of such protest is that the valuation or assessment of the property is illegal or void the board shall notify the county appraiser thereof.

(i) In the event of a hearing, the same shall be originally set not later than 90 days after the filing of the copy of the written statement of protest and a copy, when applicable, of the written notification of the results of the informal meeting with the county appraiser with the board. In all instances where the board sets a request for hearing and requires the representation of the county by its attorney or counselor at such hearing, the county shall be represented by its county attorney or counselor.

(j) When a determination is made as to the merits of the tax protest, the board shall render and serve its order thereon. The county treasurer shall notify all affected taxing districts of the amount by which tax revenues will be reduced as a result of a refund.

(k) If a protesting taxpayer fails to file a copy of the written statement of protest and a copy, when applicable, of the written notification of the results of the informal meeting with the county appraiser with the board within the time limit prescribed, such protest shall become null and void and of no effect whatsoever.

(l) In the event the board *or a court of competent jurisdiction* orders that a refund be made and no appeal is taken from such order, *or in the event of a change in valuation which results in a refund pursuant to subsection (a)*, the county treasurer shall, ~~as soon thereafter as reasonably practicable~~ *within 30 days after such order or change becomes final,* ~~refund to the taxpayer such protested taxes from tax moneys collected but not distributed. If the county treasurer fails to~~ *refund such protested taxes* ~~within 30 days, such protested taxes~~ *plus interest at the rate of 12% per annum from the date such taxes were paid or required to be paid, whichever is later,* until the date the appeal was filed with the state board of tax appeals ~~shall be refunded~~ *to the taxpayer from tax monies collected but not distributed.* However, interest shall only be assessed against the county when the county has initiated an appeal to the board or to a court of competent jurisdiction and when the board or the court has specifically found that the county's position has no basis in fact or in law and is frivolous. Upon making *any* such refund, the county treasurer shall charge the fund or funds having received such protested taxes **except that, with respect to that portion of any such refund attributable to interest, the county treasurer shall charge the county general fund.**

(m) Whenever, by reason of the refund of taxes previously received or the reduction of taxes levied but not received as a result of decreases in assessed valuation, it will be impossible to pay for imperative functions for the current budget year, the governing body of the taxing district affected may issue no-fund warrants in the amount necessary. Such warrants shall conform to the requirements prescribed by K.S.A. 79-2940, and amendments thereto, except they shall not bear the notation required by such section any may be issued without the approval of the state board of tax appeals. The governing body of such taxing district shall make a tax levy at the time fixed for the certification of tax levies to the county clerk next following the issuance of such warrants sufficient to pay such warrants and the interest thereon. All such tax levies shall be in addition to all other levies authorized by law.

(n) The county treasurer shall disburse to the proper funds all portions of taxes paid under protest and shall maintain a record of all portions of such taxes which are so protested and shill notify the governing body of the taxing district levying such taxes thereof and the director of accounts and reports if any tax protested was levied by the state.

(o) This statute shall not apply to the valuation and assessment of property assessed by the director of property valuation and it shall not be necessary of any owner of state assessed property, who has an appeal pending before the board of tax appeals, to protest the payment of taxes under this statute solely for the purpose of protecting the right to a refund of taxes paid under protest should that owner be successful in that appeal.

Sec. 2. K.S.A. 1994 Supp. 79-2005 is hereby repealed.

Sec. 3. This act shall take effect and be in force from and after its publication in the statute book.

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Johnson County
Kansas

March 9, 1995

HOUSE TAXATION COMMITTEE

HEARING ON SENATE BILL 165

TESTIMONY OF GERRY RAY, INTERGOVERNMENTAL COORDINATOR
JOHNSON COUNTY BOARD OF COMMISSIONERS

Mr. Chairman, members of the Committee, my name is Gerry Ray, representing the Johnson County Board of Commissioners. I am appearing today as a proponent of SB 165, pertaining to the payment of delinquent taxes. The bill applies only to Johnson and Wyandotte Counties.

For some background, we need to compare the time periods allowed for payment of back taxes on various types of properties. Business property is allowed two years with the prerogative to make partial payments. Abandoned property is given only one year to pay in full. Residential or homestead, as it is referred to in the statutes, is allowed partial redemption of back taxes under existing law. Partial payments must be applied to the most delinquent year, thus the taxpayer can remain in arrears interminably.

A simple explanation of the amendment proposed in SB 165, is that it stops delinquent taxpayers from taking advantage of the law by extending the three year limit for payment of delinquent tax into perpetuity. SB 165 makes a very simple change that would require any partial payment to be applied to the most recent tax delinquency. Making this change would limit delinquencies to a three year period. The amendment would require, in effect, that the taxes be current at least once every three years.

Some may feel this is a harsh and uncaring proposal that will harm property owners. Before judgments are made on that, we need to look at several factors that are relevant:

... The delinquent taxpayers are not being helped by providing them a way to remain in arrears. With the interest and penalties that accrue they can quickly get into a situation in which they can never catch up.

... When the delinquencies continue to accrue it is extremely difficult or impossible to find a lender who is willing to grant a loan or take a second mortgage to pay the back taxes.

... They are not eligible to receive assistance under the State's Homestead Property Tax Refund Act, because the Act requires that their taxes be current.

House Taxation
3-9-95
Attachment 3-1

... The property owners who pay their taxes must make up for the taxes that are not paid by the delinquent taxpayers.

When you consider the above points, you can see that retaining the current system is not actually benefiting anyone.

Recent legislative changes have recognized the needs of creditors and have shortened the redemption for certain types of foreclosures in the private sector. In 1994 a law was enacted that reduced the minimum period from six to three months to begin proceedings in the event a default occurs on a mortgage. The maximum period is twelve months. When you consider that financial institutions can take action on defaults in three to twelve months, it certainly seems reasonable that the government should be able to limit defaults on taxes owed, to a three year time frame.

Business would never be expected to permit their delinquent accounts receivable to go uncollected without an end in sight. The State does not allow people who owe income tax to continually extend their grace period. In SB 165 all we are asking is that you remove a restrictive feature from the law on local taxes and allow a timely collection of tax that is owed to the countries, cities and school districts.

Citizens are expecting governments at all levels to perform more efficiently, and operate in a more businesslike manner. We are told to do more with less and find other revenue sources to hold down taxes. SB 165 would provide a tool that would help achieve these ends.

It is sincerely hoped that after you give SB 165 serious consideration you will agree with the local officials, that it is a proposal that is reasonable and will have a positive effect.

Thank you for your time to consider this proposal and I will stand for questions.

February 20, 1995

Re: Senate Bill No. 275

Senate Taxation Committee
State Capitol, Room 519-S
Topeka, Kansas 66612

This bill will provide important instruction with regard to consideration of appraisal techniques that currently are at risk of being ignored by the Courts. The mass appraisal programs purchased by the State for reappraisal were not designed to accommodate the standard appraisal techniques applied to holdings of multiple lots, nor were all of the County Appraisers skilled in this area of valuation. As a result, many vacant lots were appraised at 5 to 10 times their market value leading directly to the bankruptcy of several developers. It is my hope that this committee recognize the validity of these techniques by including the change in language at issue, and consider further measures to insure that Administrative and Judicial bodies do not have the latitude to misconstrue statutory language in a manner that leads to a precedent for ad valorum valuation on any basis other than "fair market value".

The "fair market value" of individual lots within a larger aggregate are less than the total of the "market prices", because future dollars are worth less than present dollars, and these returns are subject to holding expenses such as taxes, sales commissions or salaries, advertising and infrastructure costs, debt service, etc. This fact has been recognized by the Federal Government and under banking guidelines, appraiser's were required to do discounted cash flow analysis in appraisal of such multiple holdings. This was to protect taxpayers and depositors against defaults that might otherwise arise from inflated opinions of value.

Without familiarity of these techniques, many County Appraisers assigned values to individual lots within larger aggregates, that reflected present "market prices" for individual lots, without deducting expenses, or anticipating the period required to market the whole, or discounting those returns to net present values. This resulted in inflated "fair market values" for the individual lots. The problem was exacerbated in some cases, when the "cost" of infrastructure still outstanding as special assessments was added to the present "market price" of each lot.

As a result, developers who had begun developments based on historic absorption trends and expenses, suddenly found themselves faced with an expense from real estate taxes that rendered many projects uneconomic, or in the best case, economic only if the absorption period could be shortened by factors that the market demand would not sustain. The options available were to appeal the valuations and hope that reason would prevail before bankruptcy was forced, or to default on the loans on the developments.

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Attachment 4-1

I was involved as an expert witness before the Kansas State Board of Tax Appeals, on a case where the methodology being used to appraise vacant lots was brought to question. The final order on the case can be found in a Board Order issued June 17, 1992, on Docket No. 89-7592-EQ, et al. On page 12, part 41. reads, "The Board concludes that the developer's discount or subdivision appraisal is an accepted mode of appraisal practice. We also conclude that the information necessary for its calculation was obtainable or was already gathered by the County Appraiser." and part 42. "The most important conclusion is whether to accept or reject the appraisal method requested...The Board concludes that the subdivision appraisal method is reasonable for subdivisions owned in common or so much of them as remains in the developer's hands."

This conclusion does little more than reaffirm the Department of Property Valuation's position that is included in a memorandum to all County Appraisers dated February 16, 1990, that reads in part, "The Vacant Lot Subcommittee of the Property Valuation Advisory Committee has spent the last few months examining the issue of subdivision development valuation. They have reached the consensus that the concept of subdivision analysis is applicable to the mass appraisal of vacant lots found in tract developments."

Though both bodies empowered with the responsibility of establishing the methodology to insure that the mandate established in KSA 79-503a to appraise all property for ad valorem purposes at "fair market value", agree that this methodology is appropriate and applicable, a case resides before the State Supreme Court that has the potential to undermine their conclusions. The seat of authority is not nearly as important in this issue as the doctrine of equalization and the essential role that "fair market value" holds in delivering that just distribution of tax burden. Without a "fair market value" standard, "just" taxation becomes subjective, and subject to arbitrary and capricious application.

In the Court of Appeals of the State of Kansas, No. 70,346, Shawnee County Appraiser, Appellant v. Lario Enterprises, Inc., Appellee, the Court states on page 1, part 3. "The developer's discount method of valuation is based upon ownership and is not based upon the value of each parcel of property as mandated by K.S.A. 1993 Supp. 79-501." The court goes on to conclude that this method leads to something other than equal treatment, and impugns the use of this method of valuation. A critical error is committed by the Court in confusing the terms "parcel" and "lot". Whereas a "lot" is a single unit within a plat, and a "parcel" as defined by the Division of Property Valuation can consist of multiple lots under common ownership, and whereas K.S.A. 79-501 establishes that Appraisers are to consider each parcel, the Court errs in concluding that each "lot" must be appraised separately under the law. They compound their error by substituting "market price" for "market value".

It is not clear whether the Court does not understand real estate appraisal, or whether they disagree that "fair market valuation" yields equal treatment in taxation and this is a studied error. In either case the doctrine of equal treatment under the law is in jeopardy without further statutory clarification.

In practice, an aggregate of lots under common holding, must be appraised using a discounted cash flow analysis. That value can then be apportioned among the lots comprising the aggregate. This practice is generally provided for through the K.S.A. 79-501 requirement that the appraiser consider each "parcel", and the definitions of "parcel" set forth by the State Division of Property Valuation in their bidder instructions to appraisal contractors. However, the DPV's definitions fall short of assuring this application to all aggregates of lots for which the method should be used. "Parcel Identification Numbers" do not cross streets, so although a developer may hold lots in several blocks within a subdivision a County Appraiser might construe that this method of valuation should be applied block by block instead of for the entire holding. In subdivisions where the developer still holds multiple lots and some lots have been isolated by improved lots, the County Appraiser may construe that the isolated lots in the active block should be treated individually instead as a part of the aggregate. In some cases an aggregate of lots are sold to a second party that is not the "developer of record", and the County Appraiser may construe that these lots should be appraised individually because they are not in the "hands of the developer". In this case the second party should be afforded the same principals of appraisal practice that the developer has, although if it is a much smaller aggregate of lots, the discounting period is likely to be shorter yielding a higher "fair market value" per lot. These are circumstances in which the discounted cash flow analysis is appropriate, but may not be understood by the County Appraisers, or specifically stated by DPV or BOTA.

If language were crafted that allowed for the appraisal of vacant lots within a subdivision under common ownership, by a discounted cash flow analysis, many of these potential problem would be eliminated. In the mean time, inclusion of the "or by absorption or sell-out period:" language proposed for K.S.A. 79-503a, would strengthen the case for "fair market value" appraisal and equal treatment in taxation.

A more detailed discussion of the particulars regarding the Appeals Court's decision with regard to "lots" and "parcel" is attached.

Sincerely,

Grant B. Gardner
Kansas State Certified Appraiser, # G-424
2305 North Richmond
Wichita, Kansas 67204

Here are my arguments against the Court of Appeals decision. I believe that the Appeals Court has raised a constitutional mandate and a statutory provision as existing in opposition to each other.

The Appeal Courts decision places the provision that mandates a "uniform and equal basis of valuation" in opposition to the requirement to appraise at "market value," when in fact if all property is appraised at "market value," the "uniform and equal basis of valuation" mandate is satisfied.

In fact the only way to insure that the mandate of a "uniform and equal basis of valuation" is to appraise all property at its "market value," or a derivative thereof, for any other valuation basis would bring in subjective elements that were not demonstrable in the real estate market and would lack a tangible benchmark that would support their uniform application.

The intent of the mandate is the fair distribution of the tax burden, and the statutory requirement to appraise at market value is the seminal genius of legislation to achieve that end.

This requirement forces that "each parcel" be taxed in proportion to a value that would be acceptable to both well informed buyer and seller acting without undue compulsion as of a common date in terms of money; and provides for a host of methods to reach this determination, and the means to test these results against actual market activities.

If this requirement is satisfied, then all have been treated in a "uniform and equal" manner. No where in the Court's decision was the valuation of the subject property found or represented to be anything other than "market value," and in this manner the property has been treated on a "uniform and equal" basis with all other property for which the requirement to appraiser at "market value" has been met.

Among the many methods of valuations that have been statutorially required for consideration in deriving "market value" is the income approach. This approach recognizes that the market places a value upon a net income stream and that for certain types of properties, the market net operating income is the principle factor in consideration of its "market value."

Because there are a variety of types of properties for which this approach is the strongest indicator of market value, and because the characteristics of these properties vary widely, the income approach also takes different forms. In all cases this approach yields a value indication that is predicated upon the current value of future net returns.

The most common form of this approach establishes a probable annual market net income, and derives a value as though the property were capable of sustaining this income into perpetuity, through the application of a capitalization rate extracted from the market for similar "investment" type properties. In function, each successive annual net income is discounted at the capitalization rate contributing a smaller percentage to current value, with the cumulative value of all returns representing the total "market value."

In other instances the income is projected for a specified period of time with the sale of the property at the end of the term. In this case the capitalization rate is translated into a "discount rate" that diminishes each year, just like in the previous case. For the final year of the term, the sale price is reduced to a current value based on the appropriate "discount factor" for that year. By example, the future returns in the 20th year using a 12% capitalization rate or "discount rate" would have a current value equal to 10.37% of its actual amount.

The income approach for development parcels, whether they be raw ground, an aggregate of lots in an active subdivision, commercial, or residential, is essentially the same as the previous case, where a capitalization rate has been converted, to discount each annual net return. Though this case involves annual returns that are not necessarily constant, the valuation technique is identical. In appraisal parlance the terms "developer discount method" or "subdivision analysis method" or "discounted cash flow analysis", speak to the application of an income approach to a particular type of property, and the term "discount" is in no way different then the reduction of future returns to current value found in any other form of the income approach.

The Appeals Court error is threefold; first they have confused "each parcel" with "each lot", second they have confused "market price" with "market value", and third they have presumed that different values constitute favoritism and hold this as antithesis to "uniform and equal basis of valuation."

The court argues that each lot should be appraised separately when the requirement is "each parcel". The definition established for "each parcel" under statutory authority of the DPV, in their bidder instructions clearly states that a parcel is a collection of lots within a subdivision held under common ownership.

In the latter case, a market value is derived for the aggregate and then allocated among the individual lots. The court has confused this allocation of the market value of the aggregate to an individual lot with the "market price" of an individual lot. The principle acting upon what the court sees as an apparent "disparity" is the size of the parcel in question and whether the market value will reflect a return over a short or long period of time.

The court has presumed that this "disparity" reflects favoritism in antithesis to "uniform and equal" treatment, when in fact if a single lot were plugged into the same analysis that was used for an aggregate of lots, the result would be a higher "market value" per lot due to fewer expenses and a quicker return, even though all were calculated using a constant market price.

All other things being equal this is "uniform and equal" treatment, with the analysis reflecting that the value per lot of a larger parcel is less than the value per lot of smaller parcel with the same density, due to increased expenses, and smaller current values associated with returns from further in the future.

These elements are reflected in real market activities conducted by informed buyers and sellers, such that two parcels varying in size, all other elements being equal including density, the smaller parcel would yield a higher price per lot sold in aggregate.
Finally, there is no evidence that an investor holding multiple lots throughout the taxing district would be subject to any less equal treatment. For each lot, the anticipated marketing time should influence its market value, and if it was not treated fairly in this fashion resulting in something other than "market value" for taxation, the owner would have cause for appeal, just as in the instant case.

Gordon T. Garrett
Vice President -
Legal Counsel

Trudy L. Perkins
Associate Director

CPAK

Commercial Property
Association of Kansas

Date: March 9, 1995

To: House Taxation Committee

From: Gordon T. Garrett, Legal Counsel
Commercial Property Association of Kansas

Subject: Senate Bill No. 275, "Fair Market Value"

Chairman, Members of the Committee, I am Gordon T. Garrett, representing the Commercial Property Association of Kansas.

We would like to support Senate Bill No. 275 because it legislatively deals with a troublesome court decision that creates major problems in the commercial development community.

Last June the Kansas Court of Appeals ruled that the appraisal method known as the Developers Discount was unconstitutional essentially because it benefitted the holders of multiple lots as opposed to the holder of a single lot, therefore violating the Kansas constitution on uniform and equal taxation.

The appraisal method of taking into account the future income of a property or properties, because not all commercial lots will be sold at the same time, is a legitimate appraisal method and should be made part of K.S.A. 79-503(a).

K.S.A. 79-503(a) list the factors to be considered in arriving at fair market value and the "absorption and sell out period" for valuing vacant commercial lots should be one of the factors.

I have attached information from the manual of the American Appraisal Institute which lays out the policy for considering future income of a property to be relative to it's valuation.

Thank you for giving us the opportunity to testify on this bill.

214 S.W. 7th Street - Topeka, KS 66603 - 913-232-048

House Taxation
3-9-95
Attachment 5-1

ket and is derived through comparable sales analysis. The income from a property, usually annual net operating income or pre-tax cash flow, is divided by its sale or equity price to obtain the income rate. A factor or multiplier can be derived by dividing a property's sale price by its annual potential or effective gross income.

Direct capitalization is market-oriented; an appraiser analyzes market evidence and values property by inferring the assumptions of typical investors. Direct capitalization does not explicitly differentiate between the return on and return of capital because investor assumptions are not specified. However, it is implied that the selected multiplier or rate will satisfy a typical investor and that the prospects for future monetary benefits, over and above the amount originally invested, are sufficiently attractive.

Direct capitalization may be applied to potential gross income, effective gross income, net operating income, or pre-tax cash flow (equity dividend). The income selected for capitalization depends on the purpose of the analysis and the data available.

Yield Capitalization

Yield capitalization is a method used to convert future benefits into present value by discounting each future benefit at an appropriate yield rate or by developing an overall rate that explicitly reflects the investment's income pattern, value change, and yield rate. Like direct capitalization, yield capitalization should reflect market behavior. The method is profit- or yield-oriented, simulating typical investor assumptions with formulas that calculate the present value of expected benefits assuming specified profit or yield requirements.

The procedure used to convert periodic income and reversion into present value is called *discounting*; the required yield rate of return is called the *discount rate*. The discounting procedure presumes that the investor will receive a satisfactory return on the investment and complete recovery of the capital invested. The method is referred to as *yield capitalization* because it analyzes whether an investment property will produce the particular level of profit or yield required. Yield capitalization is also called *discounted cash flow analysis* because a discount rate is used to calculate the present value of anticipated future cash flows.

Appraisers distinguish between contract rent and market rent in analyzing income. Market rent is used to value a fee simple estate. If a leased fee estate is being valued, the appraiser considers contract rent for the existing leases and market rent for lease renewals.

A number of analytical techniques and procedures can be used to value an entire property, specific property benefits, or partial interests in property. Present value can be calculated with or without considering the impact of financing and income taxes as long as the specific rights being appraised are clearly identified. The techniques and procedures selected are determined by the purpose of the analysis, the availability of data, and the practices common in the marketplace.

Direct Capitalization, Yield Capitalization, and Discounting Compared

Direct capitalization is simple and easily understood. The capitalization rate or factor is derived directly from the market. Direct capitalization does not require

Ref: Manual of American Appraisal Institute

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