

**THE PROPERTY TAX CRISIS, EQUITY,
AND PROPERTY TAX REFORM:
CHOOSING BETWEEN MARKET & NON-
MARKET METHODS OF VALUING THE
PROPERTY TAX BASE**

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INTRODUCTION

In 2007, many Florida residents were being priced out of their homes by increasing property taxes.¹ This occurred during the mid-2000's real estate bubble, as property taxes based on rapidly increasing real estate values rose faster than homeowner income.² One Miami homeowner, Sergio Martinez, reported to

¹ See Tim Padgett & Michael Peltier, *Behind Florida's Property Tax Revolt*, TIME, June 12, 2007, <http://www.time.com/time/nation/article/0,8599,1632143,00.htm>.

² See *id.*; see also Steven V. Melnik & David S. Cenedella, *Real Property Taxation and Assessment Processes: A Case for a Better Model*, 12 N.Y.U. J. LEGIS. & PUB. POL'Y 259, 264 (2009) ("[I]n 2000, property values began to increase dramatically just as growth in personal incomes began to slow, which once again resulted in an increase of property taxes as a percentage of personal income. These developments again sparked taxpayer anger in a manner similar to the 1970's and early 1980's."); Micah Lemons, Comment, *Circuit Breakers: Implementing a Property Tax Credit to Help Low-Income Households*, 19 GEO. J. ON POVERTY L. & POL'Y 111, 112 (2012) ("[P]roperty taxes . . . do not decrease in relation to the change[s] in income.").

Time Magazine in 2007 that he had to work two jobs in order to pay his property taxes and insurance.³

In 2004, Mr. Martinez bought his home for \$405,000 with annual property taxes of \$2800.⁴ By 2007, the value of his house had appreciated to \$900,000 and incurred \$7400 annually in property taxes.⁵ With thirty-seven percent of all Florida residents considering moving out of the state because of similar experiences, the state legislature began considering property tax reform.⁶ The legislature wanted to control escalating tax values and help keep people in their homes.⁷ Florida was not the only state facing this issue.

Then, a second financial event created a new wave of problems for property taxation: the 2008 housing market collapse. In 2008, the U.S. witnessed the largest recorded downturn in American housing price history with an eighteen percent drop in the average home price of twenty major U.S. cities.⁸ Although many expected property taxes to decrease with corresponding property values, taxes actually increased.⁹ Taxes increased because of several reasons: the time it takes for assessors to capture changing market values,¹⁰ some localities increased tax rates to make up for declining values,¹¹ and non-market based valuations.

³ Padgett & Peltier, *supra* note 1; *see also* Lemons, *supra* note 2, at 111-12 (“Unlike sales taxes and income taxes that are gradually taken out of the taxpayer’s wallet, the property tax appears in the form of a large, one-time payment.”).

⁴ Padgett & Peltier, *supra* note 1.

⁵ *Id.*

⁶ *See id.*

⁷ *See id.*

⁸ Ruth Mantell, *Home Prices Off Record 18% in Past Year, Case-Shiller Says*, MARKET WATCH (Dec. 30, 2008), http://articles.marketwatch.com/2008-12-30/finance/30729724_1_largest-price-drop-home-prices-cities. The decline in home prices was measured by the Case-Shiller price index published by Standard & Poor’s. *Id.* In 2008 alone, cities within these states experienced the following declines in property values: “Las Vegas, down 31.7%; San Francisco, down 31%; Miami, down 29%; Los Angeles, down 27.9%; San Diego, down 26.7%; . . . Tampa, down 19.8%, . . . Atlanta, down 10.5%; . . . and Dallas, down 3%.” *Id.*

⁹ Aaron Merchak & Kail Padgitt, *Fiscal Fact No. 243: Property Tax Revenue Increased As Property Values Fell*, TAX FOUND. (Aug. 31, 2010), <http://taxfoundation.org/article/property-tax-revenue-increased-property-values-fell>.

¹⁰ *Id.* at 3.

¹¹ *Id.* at 2.

The following table lists the percentage increases experienced in Florida, Nevada, Georgia, and California.¹²

	Per Capita Property Tax Collection Percentage Change 2007-2008	Nationwide Rank (1 = Largest Increase)
Florida	11.7 %	1
Nevada	9.2%	5
California	7.6%	10
Georgia	5.3%	22

As a result of the three market events mentioned above, property tax valuations have remained higher than their actual market worth. In 2011, foreclosures continued to drive market values down. Currently, many taxpayers simply cannot afford taxes based on values higher than their property's actual worth. Record numbers of property tax appeals are forcing state legislatures across the country to reevaluate current property taxation methods to provide relief.

Now several states are considering or have begun reforming their property tax systems.¹³ Generally, these reform measures seek to limit and reduce property taxation. This comment focuses on California, Florida, Georgia, and Nevada for two reasons: each of these states experienced inflated real estate prices throughout the housing bubble, and these states have enacted legislation to limit property tax increases that occur as a result of rapid increases in real estate prices. This Comment does not address every criticism of property tax, or every attempt at property tax

¹² *Id.* at 1-2.

¹³ See Eric Boehm, *Property Tax Reform Final Piece of State Budget*, PA. INDEP., July 1, 2011, <http://paindependent.com/2011/07/property-tax-reform-final-piece-of-state-budget/>; Cara Matthews, *Report: 74 Percent of N.Y. Schools Would Exceed Property Tax Cap*, COURIER-J., Dec. 14, 2011, <http://www.courier-journal.com/article/CB/20111214/NEWS01/112140352/Report-74-percent-N-Y-schools-would-exceed-property-tax-cap>; Rob Scott, *Christie Makes Mt. Laurel Appearance Touting Property Tax Reform*, MOORESTOWN PATCH, Oct. 13, 2011, <http://moorestown.patch.com/articles/christie-makes-mt-laurel-appearance-touting-property-tax-reform>.

reform.¹⁴ The purpose of this Comment is to inform legislatures considering reform because of the problems caused by the recent housing bubble and its collapse. It advocates market value based property taxation to achieve equality in the distribution of the property tax burden.

Part I of this Comment is a general introduction to how property taxes are calculated and the three types of valuation. Part II discusses the drawbacks of non-market valuation methods. Part III discusses legislative reform in Georgia and Florida. Part IV demonstrates how reform in Georgia and Florida has solved the insulation and efficiency problems with market valuation.

I. REAL PROPERTY TAXATION: METHODS OF VALUATION

Determination of value is the main focus of this Comment. The three methods of determining value for property taxation are: (1) market valuation, (2) acquisition valuation, and (3) taxable-valuation. County tax assessors appraise properties within their jurisdiction's tax base and their appraisal sets the property's value. While the method of determining value depends on the state, the overall formula for taxation is generally the same. The following section discusses basic property tax computation. Then, a discussion of each method of valuation follows.

A. Property Taxation Generally

The following table illustrates the general formula used to tax property where the value of a particular property is \$100,000. The percentage and millage rate in the example are not representative of any particular state or county. "[T]he market value of property, as determined by the assessor, is not the actual tax base used in computing the property tax. Instead, the market value is multiplied by an 'assessment ratio' to determine the taxable-value (also referred to as 'assessed value')."¹⁵

¹⁴ For an exhaustive discussion of property tax reform, please see Melnik & Cenedella, *supra* note 2.

¹⁵ *Id.* at 273 ("The most common purpose of applying an assessment ratio of less than one hundred percent is that, when combined with a classification system, states may reduce that actual tax bill for residential properties in comparison to commercial properties.").

Market Value	\$ 100,000
x %	x 35%
Assessed Value	35,000
<u>x Millage Rate</u>	<u>x .0320</u>
Taxes Due	\$1,120.00 ¹⁶

Understanding this formula helps illustrate the important relationship between value and the millage rate (or the tax rate). That is, taxes due can be kept constant by adjusting the millage rate to offset changes in value. The following example illustrates this point:

Value	\$100,000	\$125,000	\$75,000
x Millage Rate	x .030	x .024	x .040
Taxes Due	\$3,000	\$3,000	\$ 3,000

A tax digest, or tax roll, is the summation of the value of all taxable property within a taxing jurisdiction. The amount of property tax revenue a locality receives is generated using the same basic formula:

$$\text{Tax Digest} \times \text{Millage Rate} = \text{Annual Property Tax Revenue}$$

Therefore, as overall values cause the tax digest to increase or decrease, the millage rate can be adjusted to keep revenue stable. The millage rate is set annually by “policymakers—school boards, city councils, [and] county commissioners . . . based on their budgetary needs.”¹⁷ “To determine the tax rate, each taxing jurisdiction determines the total amount of taxes it needs to raise and then divides that number by the total taxable assessed values within the jurisdiction, subject to certain constitutional restrictions.”¹⁸ So Florida’s 2007 property tax problem described

¹⁶ NEV. TAXPAYERS ASS’N, UNDERSTANDING NEVADA’S PROPERTY TAX SYSTEM 12 (2011-2012 ed.), available at www.nevadataxpayers.org (follow “Property Tax” hyperlink; then follow “Understanding Nevada’s Property Tax System” hyperlink).

¹⁷ NAT’L CONFERENCE OF STATE LEGISLATURES, A GUIDE TO PROPERTY TAXES: THE ROLE OF PROPERTY TAXES IN STATE AND LOCAL FINANCES 13 (2004), available at <http://www.ncsl.org/issues-research/budget-tax/property-taxes.aspx>.

¹⁸ Melnik & Cenedella, *supra* note 2, at 274.

in the Introduction could have been avoided if local governments had simply reduced the millage rates as the tax digest increased.

B. Market Valuation

The most prominent method used to determine value is market valuation. For the purposes of this Comment, it is discussed as implemented in Florida and Georgia.¹⁹ Market valuation determines the fair market value of property, which is “the amount a knowledgeable buyer would pay for the property and a willing seller would accept for the property at an arm’s length, bona fide sale.”²⁰

1. Three Approaches to Market Valuation

Market valuation is a reconciliation of three determinations of value.²¹ To find the fair market value of the subject property (or the property being assessed) the cost, sales comparison, and income approach are used.²² Florida publishes the *Real Property Guidelines*, which succinctly summarize the three different approaches.²³ These guidelines are consistent with the *Uniform Standards of Professional Appraisal*.²⁴

First, the cost approach determines the value of the subject property by adding the value of the land to the value of the improvements on the land, less their depreciation.²⁵ The theory is that the value of a property can be determined by the cost of a similar substitute property.²⁶ The improvements are valued at their reproduction cost new, and then the accrued depreciation is subtracted.²⁷

¹⁹ See FLA. STAT. ANN. § 192.001(2) (West 2011); GA. CODE ANN. § 48-5-6 (2010).

²⁰ GA. CODE ANN. § 48-5-2(3) (2010).

²¹ See UNIF. STANDARDS OF PROF'L APPRAISAL PRACTICE U20-21 (2010-2011).

²² *Id.*; see also FLA. STAT. ANN. § 193.011 (West 2011); GA. CODE ANN. § 48-5-2 (2010).

²³ FLA. DEP'T OF REVENUE PROP. TAX ADMIN. PROGRAM, FLORIDA REAL PROPERTY APPRAISAL GUIDELINES 37-49 (2002), available at <http://dor.myflorida.com/dor/property/rp/pdf/FLrpg.pdf>.

²⁴ See UNIF. STANDARDS OF PROF'L APPRAISAL PRACTICE U16-21 (2010-2011).

²⁵ FLORIDA REAL PROPERTY APPRAISAL GUIDELINES, *supra* note 23, at 37.

²⁶ *Id.* at 37-41.

²⁷ *Id.* at 37.

Second, the sales comparison approach is a method of estimating the price “where the results of arm’s length sales transactions . . . are analyzed for just value indications, which then may be applied to all properties within such groups.”²⁸ Value is estimated by gathering data on all arms-length transactions similar to the subject property.²⁹ Each comparable sale is then adjusted for value differences from the subject property.³⁰ Finally, the appraiser compiles the values of all of the comparable properties, assigning the greatest weight to those that are the most similar.³¹

Third, is the income approach which is “a set of procedures where stabilized income from income-producing real property is capitalized into a just value indication.”³² Value is derived by estimating the annual gross income less the annual expenses for the property.³³ This generates the annual net operating income (NOI), which is then capitalized.³⁴ Capitalization divides the NOI by a capitalization rate which yields the value of the property.³⁵

To arrive at the ultimate estimate of value, the appraiser must reconcile the approaches used.³⁶

2. Advantages and Disadvantages of Market Valuation

Market valuation has many positive aspects. Taxation based on a property’s fair market value makes tax liability a function of market worth, and therefore what taxpayers can afford to purchase. Market valuation also provides a non-arbitrary method of valuing real estate because it is computed using the method described in the previous section.³⁷

Most importantly, market valuation is equitable. Market valuation is based on market price data and reflects changes

²⁸ FLORIDA REAL PROPERTY APPRAISAL GUIDELINES, *supra* note 23, at 42.

²⁹ *Id.*

³⁰ *Id.* at 42-43.

³¹ *Id.* at 42-44.

³² *Id.* at 44.

³³ *Id.*

³⁴ *Id.*

³⁵ *Id.*

³⁶ See UNIF. STANDARDS OF PROF'L APPRAISAL PRACTICE U20 (2010-2011).

³⁷ See *supra* notes 16-32 and accompanying text.

within the real estate market.³⁸ Similar properties within a market should have similar fair market values and similar tax bills. Therefore, market valuation proportionately distributes the tax burden because tax liability is proportionate to property value.

Supporters of non-market methods argue that taxation based on market valuation is actually more disparate than equitable.³⁹ Often, the lag between market changes and the time it takes to gather data and complete an appraisal results in outdated valuations.⁴⁰ “Longer assessment cycles can be troublesome when property values increase rapidly because several years of property appreciation can cause large increases in property taxes.”⁴¹ Incorrect valuations mean that until a new appraisal is completed, some taxpayers pay either too little or too much in property taxes.⁴² Two years is the estimated amount of time that it takes for a geographic area to capture changes in that market.⁴³

Market valuation requires a lot of data and individual review by appraisers in periods of slow market growth.⁴⁴ Dramatic changes in the real estate market have an even worse effect on market valuation output because the data is constantly changing.

³⁸ See UNIF. STANDARDS OF PROF'L APPRAISAL PRACTICE U16-20 (2008-2009).

³⁹ See *Proposition 13: Love it or Hate it, its Roots Go Deep*, CAL-TAX RES. (Nov. 1993) [hereinafter *Proposition 13*], <http://www.caltax.org/research/prop13/prop13.htm>; see also Darien Shanske, *What the Original Property Tax Revolutionaries Wanted (and It is Not What You Think)*, 1 CAL. J. OF POL. & POL'Y 1, 16 (2009) (reviewing ISAAC W. MARTIN, *THE PERMANENT TAX REVOLT: HOW THE PROPERTY TAX TRANSFORMED AMERICAN POLITICS* (2008)).

⁴⁰ See Justin Higginbottom, *Fiscal Fact No. 223: State Provisions for Property Reassessment*, TAX FOUND. (Apr. 29, 2010), <http://taxfoundation.org/article/state-provisions-property-reassessment>.

⁴¹ Melnik & Cenedella, *supra* note 2, at 267-68. Melnik & Cenedella note:

For example, the median selling price for residential property in the United States rose over thirteen percent from 2003 to 2004 and over eight percent from 2004 to 2005. To the extent that real property is not reassessed, it does not reflect the change in property values due to market forces. In a period of increasing home values, assessed values will lag behind current market values, resulting in a lower tax base than if properties were reassessed annually.

Id. (citation omitted).

⁴² Higginbottom, *supra* note 40, at 1.

⁴³ Shanske, *supra* note 39, at 16.

⁴⁴ See *supra* notes 16-32 and accompanying text.

This is why, since 2006, reassessments in many states have not been able to reflect accurate values in their tax bills.⁴⁵

A second critique of market valuation is that it does not insulate taxpayers from market changes.⁴⁶ Recently, taxpayers in the U.S. experienced this during the housing bubble. As the real estate market dramatically increased in the 2000s so did corresponding tax valuations and property tax bills.⁴⁷ In 2005, data showed that the average nationwide home price had increased fifty percent in five years, doubled in some cities, and this ultimately did not peak until 2007.⁴⁸

The problem is that even as homeowners experience increasing equity in their property, their income does not increase.⁴⁹ Therefore, they cannot afford higher property taxes based on the increases in value. Moreover, the 2000 housing bubble is not the first time property owners have been gouged by market prices. Rapidly increasing property values in the 1970s also led to steep increases in property taxes. In response, certain states “revolted” against market valuation and adopted non-market based methods.⁵⁰ Those methods are discussed in the following section.

C. Acquisition Valuation

Acquisition valuation is only used in California.⁵¹ Proposition 13 is the amendment that created acquisition valuation. The Proposition was adopted by voters in 1978 to limit property tax liability.⁵² Before Proposition 13, real property in California was taxed using market valuation.⁵³ Increasing property values

⁴⁵ *Id.*

⁴⁶ See Shanske, *supra* note 39, at 16; see also Lemons, *supra* 2, at 111 (“[A]ssessment values tend to rise rapidly in some areas, furthering the taxpayer’s sense of unfair application.”).

⁴⁷ See Padgett & Peltier, *supra* note 1.

⁴⁸ Graham Searjeant, *US Heading for House Price Crash, Greenspan Tells Buyers*, SUNDAY TIMES, Aug. 27, 2005.

⁴⁹ See Padgett & Peltier, *supra* note 1.

⁵⁰ *Proposition 13*, *supra* note 39.

⁵¹ *Id.*

⁵² *Id.*

⁵³ CAL. STATE BD. OF EQUALIZATION, CALIFORNIA PROPERTY TAX: AN OVERVIEW (Aug. 2009), available at <http://www.boe.ca.gov/proptaxes/pdf/pub29.pdf>.

caused property taxes to rise dramatically and created local government surpluses.⁵⁴

The adoption of Proposition 13 was a solution for taxpayers who wanted insulation from volatility in real estate market prices.⁵⁵ The line of thinking was: “Why should I be priced out of my home on account of a spike in my property taxes because some person is willing to pay a huge premium for my house . . . ?”⁵⁶ In order to limit property tax liability Proposition 13 changed California’s valuation method from market valuation to acquisition valuation.⁵⁷

First, property values were rolled back to 1975 values to account for the recent inflation spikes that had caused values to increase.⁵⁸ After setting the “base year” amount a property’s value can only be adjusted by either the rate of inflation or two percent annually, whichever is less.⁵⁹ A new base year valuation is triggered by only two events: a change in ownership⁶⁰ or completion of new construction, thus the name “acquisition value.”

⁵⁴ *Id.*; see also *Proposition 13*, *supra* note 39. Recall that as a property’s value increases so does its tax liability. See *supra* note 16 and accompanying table.

⁵⁵ See Shanske, *supra* note 39, at 15-16. Many now consider it popular wisdom that at least part of the support for Proposition 13 was actually in response to California Supreme Court decisions that equally distributed local finances among school districts. *Id.* at 1-2.

⁵⁶ *Id.* at 16. Property owners’ fear of losing their homes was not an exaggeration in the market of the 1970s. See *Proposition 13*, *supra* note 39. Just like the scenario in Florida, property taxes could have been kept in check if millage rates had been lowered in response to the rising values, but they were not.

⁵⁷ CAL. STATE BD. OF EQUALIZATION, *supra* note 53. In the first year of its adoption, Proposition 13 caused property tax revenues to drop by \$5.26 million and created a “fiscal crisis” for local governments. *Id.*

⁵⁸ *Id.* at 14. Due to California’s legislative scheme this was accomplished by amending the state Constitution. Melnik & Cenedella, *supra* note 2, at 264. The amendment is significant because it nullifies the typical requirement that taxpayers be taxed equally. This equality argument is what was presented to the United States Supreme Court in *Nordlinger v. Hahn*, 505 U.S. 1 (1992). See *infra* note 78 and accompanying text.

⁵⁹ See CAL. STATE BD. OF EQUALIZATION, *supra* note 53. The term “base year value” is interchangeable with “assessed value.” *Id.* at 10.

⁶⁰ See *id.* at 1. The change in ownership requirement is more easily avoided by commercial property owners than residential. See CAL. TAX REFORM ASS’N, RECOMMENDATIONS TO ACHIEVE REVENUE SUFFICIENCY (Jan. 12, 2011), available at <http://www.ccrwf.org/wp-content/uploads/2011/01/ctrarevenuerrecommendations-wfsummit2011-final.pdf>. “Due to the complexity of commercial property ownership (LLC’s REIT’s, partnerships, private equity holdings, trusts, etc), [identifying changes

The tax burden for the entire ownership period is based on only the market price at the time the property was sold or built. So, long-term property owners have a huge tax advantage in an increasing market because they are locked in at a base value that can only increase by two percent at the most.⁶¹ “The longer one stayed in one’s home, the less one’s total property tax burden became relative to the home’s true value.”⁶² This tax advantage, referred to as “the privilege,” does not transfer to new owners. When property is sold the purchase price becomes the tax assessor’s new base year value and the new owner is taxed on that until they sell.

D. Taxable-Valuation

Another non-market property valuation method is Nevada’s taxable-valuation. Nevada is the only state in the country that uses this method.⁶³ Like Proposition 13, taxable-value was adopted in response to rapidly increasing property taxes in the 1980s.⁶⁴ The formula for taxable-value is:

$$\text{Taxable-Value} = \text{Land's Full Cash Value} + (\text{Replacement Cost New of Improvements} - (1.5\% \text{ Depreciation} \times \text{Life of Improvement}))$$

Taxable-value is similar to market valuation’s cost approach. The appraiser determines the “full cash value” of the land, which is “[t]he most probable price [that the] property would bring in a competitive and open market under all conditions requisite for a fair sale.”⁶⁵ Any improvements on the subject property are valued by estimating the cost to replace them regardless of their current

in ownership using] this approach is confusing, unenforceable, and full of loopholes.” *Id.* Notably, “California is the only state in the nation that assesses commercial property based on a change of ownership.” *Id.*

⁶¹ CAL. STATE BD. OF EQUALIZATION, *supra* note 53.

⁶² Shanske, *supra* note 39, at 3.

⁶³ John Dougherty, *Property-Tax Conflict Enters Nevada Governor’s Race*, N. LAKE TAHOE BONANZA, Jan. 28, 2010, <http://www.tahoebonanza.com/apps/pbcs.dll/article?AID=/20100128/NEWS/100129889&template=printart>.

⁶⁴ *Id.*

⁶⁵ NEV. TAXPAYERS ASS’N, *supra* note 16, at 2.

zoning or use (this is referred to as the replacement cost new).⁶⁶ The replacement cost new is then depreciated at 1.5% for each year of the improvement's life.⁶⁷ In Nevada appraisers are required to revalue property every five years.⁶⁸

In addition to taxable-valuation, the Nevada legislature capped the amount that property tax bills can increase in a tax year.⁶⁹ Similar to the situation described in Florida in 2007, 2004 projections showed that homeowners could face twenty to fifty percent increases in their tax bill.⁷⁰ The Nevada legislature placed a cap on property tax bills.⁷¹ Total residential property tax bills may not increase by more than three percent annually and commercial bills are limited to eight percent increases.⁷²

II. PROBLEMS WITH NON-MARKET VALUATION: EQUITY, COMPLEXITY, AND THE REALITY OF A DECLINING MARKET

Acquisition and taxable-valuation were designed to benefit taxpayers by insulating property taxes from market volatility. However, there are three major criticisms of these non-market methods. First, acquisition valuation does not equitably distribute the tax burden among similar properties. Second, taxable-valuation can be extremely complex to implement. And third, the current decline in real estate values frustrates the goals of both acquisition and taxable-valuation.

A. Acquisition Valuation Provides the Most Benefit to Long-Term Property Owners and Commercial Property

California openly acknowledges that the acquisition system creates disparities in the distribution of the tax burden:⁷³

⁶⁶ NEV. REV. STAT. ANN. § 361.227(1)(b) (West 2011). Depreciation "is the estimate of the decrease in value in a wasting asset (not land) due to such factors as use and obsolescence." NEV. TAXPAYERS ASS'N, *supra* note 16, at 2.

⁶⁷ NEV. TAXPAYERS ASS'N, *supra* note 16, at 2.

⁶⁸ *Id.* at 7.

⁶⁹ Sean Whaley & Erin Neff, *Pact Sets Cap on Property Tax Bills*, LAS VEGAS REV. J., Apr. 1, 2005, http://www.reviewjournal.com/lvrj_home/2005/Apr-01-Fri-2005/news/26198530.html.

⁷⁰ *Id.* This was also an attempt to ward off Proposition 13-like initiatives. *Id.*

⁷¹ Nev. Assemb. B. 489, 73d Reg. Sess. (Nev. 2005).

⁷² *Id.*

⁷³ See CAL. STATE BD. OF EQUALIZATION, *supra* note 53.

[S]imilar properties can have substantially different assessed values based solely on the dates the properties were purchased. . . . Longtime property owners, whose assessed values generally may not be increased more than [two] percent per year, tend to have markedly lower tax liability than recent purchasers, whose assessed values tend to approximate market levels.⁷⁴

Recall that the goal of acquisition value and Proposition 13 was to insulate taxpayers from market conditions that caused valuations and property taxes to rapidly increase.⁷⁵ Also, recall that this is accomplished by setting the base year valuation at the property's purchase price, and only increasing that base value by either two percent or the annual rate of inflation.⁷⁶ As long as annual property appreciation is less than two percent, taxpayers have a lower tax valuation than what their property is worth in the market. The longer one stays in one's home, the greater the tax savings they will experience over time. Therefore, two homes with exactly the same fair market value will have different property taxes because of the year in which they were purchased.⁷⁷

The United States Supreme Court held that disparity in tax liability for similar properties does not violate the Equal Protection Clause.⁷⁸ The Court did not find that acquisition value is a fair or effective method of taxation.⁷⁹ Instead, the decision is an example of the Court refusing to enforce economic substantive due process among the states.⁸⁰

⁷⁴ *Id.* Notably California taxpayers are allowed to make market value arguments when they appeal their assessments. CAL. STATE BD. OF EQUALIZATION, RESIDENTIAL PROPERTY ASSESSMENT APPEALS 1, 3 (March 2003), <http://www.boe.ca.gov/proptaxes/pdf/pub30.pdf>. Local county appeals boards are allowed to raise or lower valuations, but not purely based on unequal taxes between neighbors. *Id.* at 1-2. Property owners can file a "decline in value" appeal to argue that their market value has fallen below the base year or assed value. *Id.* at 3. Admissible evidence to support this type of appeal is a market value sales comparison approach. *Id.* at 9-12.

⁷⁵ *See supra* notes 51-56 and accompanying text.

⁷⁶ *See supra* notes 58-61 and accompanying text.

⁷⁷ *See* CAL. STATE BD. OF EQUALIZATION, *supra* note 53.

⁷⁸ *Nordlinger v. Hahn*, 505 U.S. 1, 17-18 (1992) (applying rational basis review).

⁷⁹ *Id.* at 12-13.

⁸⁰ *See Williamson v. Lee Optical of Okla.*, 348 U.S. 483, 488 (1955) (citing *Day-Brite Lighting, Inc., v. Mo.*, 342 U.S. 421 (1952); *Daniel v. Family Sec. Life Ins. Co.*, 336 U.S. 220 (1949); *Lincoln Fed. Labor Union No. 19129, A.F. of L. v. Nw. Iron & Metal*

California taxpayers accept disproportionate taxes because of the “privilege” created by Proposition 13. Tax savings given to long-time property owners whose tax valuations are never brought up to market value fuels continued support for acquisition valuation. “The entire scheme is cyclical in nature though, because as long as property values continue to rise, last year’s newcomers will always be better off than the current year’s newcomers, and so on.”⁸¹

Additionally, acquisition valuation benefits commercial property owners more than homeowners.⁸² In 1975, in Los Angeles County, residential property paid fifty-three percent of property taxes, and commercial property paid forty-six percent.⁸³ Today, residential pays sixty-nine percent and commercial only pays thirty percent.⁸⁴ One reason for the disparity is because homes generally sell more frequently than commercial property, so they have more frequent changes in their base year valuations than commercial real estate.⁸⁵ Partnerships, REITs, and LLCs also provide loopholes to acquisition reassessment.⁸⁶ Overall, residential property carries more tax burden than commercial.⁸⁷

B. The Limited Insulation Provided by Taxable-Valuation is Outweighed by its Complexity

Taxable-valuation insulates taxpayers from market volatility by using a fixed rate of depreciation. However, the degree of insulation is much less than acquisition value because market

Co., 335 U.S. 525 (1949); *Olsen v. Neb. ex rel. W. Reference & Bond Ass’n*, 313 U.S. 236 (1941); *W. Coast Hotel Co. v. Parrish*, 300 U.S. 379 (1937); *Nebbia v. New York*, 291 U.S. 502 (1934)) (“The day is gone when this Court uses the Due Process Clause of the Fourteenth Amendment to strike down state laws, regulatory of business and industrial conditions, because they may be unwise, improvident, or out of harmony with a particular school of thought.”).

⁸¹ Melissa J. Morrow, *Twenty-Five Years of Debate: Is Acquisition-Value Property Taxation Constitutional? Is it fair? Is it Good Policy?*, 53 EMORY L.J. 587, 596 (2004).

⁸² See Steve Lopez, *It’s Time to Tinker with ‘Untouchable’ Prop. 13*, L.A. TIMES, Apr. 02, 2011, <http://articles.latimes.com/2011/apr/02/local/la-me-0403-lopez-prop13-supporters-20110328>.

⁸³ *Id.*

⁸⁴ *Id.*

⁸⁵ *Id.*

⁸⁶ See *id.*

⁸⁷ *Id.* Contrast with Proposition 13’s original goal of providing tax relief to California homeowners. See *supra* notes 51-57 and accompanying text.

data dictates raw land and improvement values. Recall that taxable-value is the sum of the full cash value of land plus the replacement cost of improvements less 1.5% depreciation for the age of the structure.⁸⁸

Taxable-valuation is difficult to implement when raw land sales are scarce. Declining land sales impair an appraiser's ability to compute full cash value. *State ex rel. State Board of Equalization v. Bakst* illustrates the effect of sales data on taxable-valuation.⁸⁹ The plaintiffs in that case were seventeen taxpayers who owned property near Lake Tahoe, Nevada.⁹⁰ The taxpayers began to question the county appraiser's methods after they received extremely high bills for the 2003-2004 tax year.⁹¹

The Nevada Supreme Court found that the appraisals violated Article 10 of the state Constitution requiring uniform and equal rate of assessment.⁹² County appraisers must use the sales data to estimate the full cash value of land.⁹³ However, the state Tax Commission did not instruct assessors on how to compute the full cash value when comparable sales data was not available.⁹⁴ Therefore, the appraisers adopted their own methods to determine full cash value.⁹⁵

Washoe County, where the plaintiff's properties were located, refunded the difference between the tax bills paid and what they should have been, plus interest.⁹⁶ After *Bakst*, Washoe County was forced to change the values of 8700 other properties to

⁸⁸ See *supra* notes 64-68 and accompanying text.

⁸⁹ *State ex rel. Bd. of Equalization v. Bakst*, 148 P.3d 717 (Nev. 2006).

⁹⁰ *Id.* at 719.

⁹¹ *Id.*

⁹² *Id.* at 721. The state Constitution provides:

The legislature shall provide by law for a uniform and equal rate of assessment and taxation, and shall prescribe such regulations as shall secure a just valuation for taxation of all property, real, personal and possessory, except mines and mining claims, which shall be assessed and taxed only as provided in section 5 of this article.

NEV. CONST. art. X, § 1.

⁹³ *Bakst*, 148 P. 3d at 722.

⁹⁴ See *id.* at 725.

⁹⁵ *Id.*

⁹⁶ *Id.* at 726.

equalize taxation for the year.⁹⁷ The total cost of the incorrect valuations plus interest on those payments was about \$40 million.⁹⁸

C. The Declining Real Estate Market Frustrates the Goals of Acquisition and Taxable-Valuation

Huge increases and decreases in California property values caused by the housing bubble have affected the acquisition value in two ways.⁹⁹ First, as turnover increased during the housing bubble the Proposition 13 privilege became less valuable. This is “because . . . homeowners have been in their homes for a shorter time and thus have benefited less from having their assessed values kept below market.”¹⁰⁰

Second, a declining market reverses the acquisition value “privilege.”¹⁰¹ Median California home prices fell over thirty percent in 2008.¹⁰² Acquisition value was designed to insulate property owners in an increasing market.¹⁰³ “Because under Proposition 13 the assessed value of property is reset at its acquisition value, the taxpayers who purchased new homes this year are going to pay *lower* property taxes than many of their neighbors in similar homes.”¹⁰⁴ If a taxpayer purchased property at the height of the real estate bubble, the base year valuation is higher than the property’s value after 2008. As long as property values continue to decrease, acquisition valuation will reward the most recent purchaser instead of the long-time property owner.

Taxable-valuation is losing support because of declines in real estate values. The preceding section describes the problems caused by decreased land sales. Taxpayers are also becoming

⁹⁷ Vill. League to Save Incline Assets, Inc. v. State ex rel. Bd. of Equalization, 194 P.3d 1254, 1256 (Nev. 2008).

⁹⁸ Susan Voyles, *Blame Follows \$40M Tax Fiasco in Incline*, RENO GAZETTE-J., Aug. 1, 2011, <http://www.rgj.com/article/20110802/NEWS/107310370/Special-Report-Blame-follows-40M-tax-fiasco-Incline>.

⁹⁹ See Shanske, *supra* note 39, at 20-23.

¹⁰⁰ *Id.* at 21.

¹⁰¹ *Id.* at 19.

¹⁰² *Id.* at 20.

¹⁰³ See *supra* notes 51-57 and accompanying text.

¹⁰⁴ Shanske, *supra* note 39, at 20.

frustrated by the caps on their total tax bills.¹⁰⁵ The market shift from rapidly increasing to decreasing has a surprising effect on capped taxes.¹⁰⁶ As property values fall, total tax bills can still increase by three percent annually under the cap.¹⁰⁷ The following table shows how taxes can still increase with the cap as values decline:

	2004	2005	2006	2007
Home Value	\$100,000	\$150,000	\$250,000	\$200,000
Assessed Value (% 35)	\$35,000	\$52,500	\$87,500	\$70,000
Taxes Billed without Cap	\$1,120	\$1,680	\$2,800	\$2,240
Taxes Billed with the 3% Cap	\$1,120	\$1,153.60	\$1,188.21	\$1,223.85 ¹⁰⁸

Finally, the current decline in real estate values probably provides the best opportunity to transition from non-market valuations.¹⁰⁹ Increasing the value of the property tax base would provide much needed revenue for local governments. California alone estimated a forty billion dollar deficit for fiscal years 2011 and 2012.¹¹⁰

The next section explains current legislative reform in two states that use market analysis to value property. These reforms demonstrate how Florida and Georgia have addressed the

¹⁰⁵ See *supra* notes 69-72 and accompanying text.

¹⁰⁶ See NEV. TAXPAYERS ASS'N, *supra* note 16, at 13.

¹⁰⁷ *Id.*; see also Dougherty, *supra* note 63.

¹⁰⁸ NEV. TAXPAYERS ASS'N, *supra* note 16, at 13.

¹⁰⁹ See Shanske, *supra* note 39, at 22-23.

¹¹⁰ *Id.* at 19 n.31.

problems with market analysis while preserving uniformity and equality in assessments.

III. MARKET VALUATION REFORM

Lack of insulation from market volatility and inefficient valuations led to property tax reform in Georgia and Florida. In 2007, some Florida homeowners experienced more than a 100% increase in their property taxes.¹¹¹ Many Florida residents could no longer afford their property taxes and were in danger of losing their homes because incomes were not increasing as fast as the housing values and corresponding tax bills.¹¹² Therefore, the Florida legislature began discussing property tax reform in 2007.¹¹³

Then, in 2008, property values fell nationwide by about sixteen percent.¹¹⁴ However, property tax collections rose nationwide by four percent.¹¹⁵ The explanation is a lag between market changes and valuation adjustments because of the time it takes to gather and input market data.¹¹⁶ However, this housing market crash occurred at the same time as a nationwide recession.¹¹⁷ Many taxpayers could not afford to wait for tax valuations to catch up with the market.¹¹⁸ Therefore, Florida and Georgia began additional reform measures in response to the downturn in 2008.

¹¹¹ Padgett & Peltier, *supra* note 1. It is important to understand that while the end result (property value increases) was similar in Florida and California, the cause was not. The main cause for California's real estate price increases in the 1970s was inflation, while the mid-2000 cause of real estate price increases was the housing bubble. *See id.*; *see also Proposition 13, supra* note 39 (explaining the cause of Proposition 13).

¹¹² *See* Padgett & Peltier, *supra* note 1.

¹¹³ *Id.*

¹¹⁴ Merchak & Padgitt, *supra* note 9, at 1.

¹¹⁵ *Id.* In 2008, Florida had the nation's highest property tax revenue increase at 11.7%. *Id.* Georgia was ranked twenty-second in the nation with a 5.3% increase in 2008. *Id.*

¹¹⁶ *Id.* at 3. Although some local governments did raise tax rates in 2008 to offset their decreasing digests, this also caused increased taxes. *Id.*

¹¹⁷ *See* Mantell, *supra* note 8; Merchak & Padgitt, *supra* note 9, at 1.

¹¹⁸ *See* Padgett & Peltier, *supra* note 1.

A. Reform in Georgia

In 2009, the *Atlanta Journal-Constitution* published an article reporting the findings of an eight-month study of property sales and their respective tax assessment values in Cobb, DeKalb, Fulton, and Gwinnett counties.¹¹⁹ The study revealed that despite the dramatic downturn in property values, property tax assessments remained higher than the statewide decrease in property values.¹²⁰ In places where median sales had fallen more than thirty percent, the corresponding median tax appraisal had only dropped between five and ten percent.¹²¹

A report by the Atlanta Neighborhood Development Partnership was introduced which studied the fifteen zip codes with the highest rate of foreclosures.¹²² It also showed that these same fifteen zip codes amount to an estimated \$118.5 million in property tax overpayment.¹²³ However, some suggested that values are just declining too fast for appraisers to catch up until the market stabilizes.¹²⁴

In response to increasing unhappiness among taxpayers, in 2009 the Georgia Senate created the Senate Study Committee on Property Tax Assessments and Appeals to study the current method of assessing real property in Georgia and recommend appropriate reform.¹²⁵ Some reasons for creating the study were:

¹¹⁹ See Ernie Suggs, *Senate Bill Would Overhaul Georgia Property Tax System*, ATLANTA J.-CONST., Feb. 1, 2010, <http://www.ajc.com/news/georgia-politics-elections/senate-bill-would-overhaul-288459.html>.

¹²⁰ *Id.*; see also PROP. TAX ASSESSMENTS & APPEALS STUDY COMM., FINAL REP., S. 150, Reg. Sess., at 10-11 (Ga. 2009).

¹²¹ Suggs, *supra* note 119.

¹²² PROP. TAX ASSESSMENTS & APPEALS STUDY COMM., FINAL REP., S. 150, Reg. Sess., at 10-11 (Ga. 2009).

¹²³ *Id.*

¹²⁴ See *Id.* at 13.

¹²⁵ See S. Res. 685, 150th Gen. Assemb., Reg. Sess. (Ga. 2009). In 2009, Georgia House Bill 233 created a moratorium to prevent an increase in assessment values for properties subject to ad valorem taxes until January 2011. See GA. CODE ANN. § 48-5B-1(b) (2009) (effective Jan. 1, 2010; repealed Jan. 10, 2011); see also PROP. TAX ASSESSMENTS & APPEALS STUDY COMM., FINAL REP., S. 150, Reg. Sess., at 6 (Ga. 2009). This was an initial attempt to provide relief to taxpayers at the beginning of the recession. But the moratorium does not apply to counties that performed a reevaluation of all their properties in 2008, preparing to revalue at the beginning of 2009, or that have a millage rate cap. *Id.* Additionally, evidence was presented that more counties than originally planned are claiming an exemption to the moratorium.

the economic downturn, increasing foreclosures, declining property values, the discrepancy between assessed values and what homeowners could realistically expect to get on the market, and taxpayers' need to have their tax burden reduced.¹²⁶

1. Senate Bill 346 Increases Efficiency and Accuracy in Market Valuation

Two main concerns of the study were how to bring the falling values and assessments in check and how to make the appeal process more efficient. In order to bridge the gap between plummeting home values and assessments, it was suggested that bank sales and foreclosure sales be included in the comparable sales analysis.¹²⁷ Although, not generally considered an arm's length transaction, bank and foreclosure sales are becoming more commonplace since the housing bubble burst.¹²⁸ Now, bank and foreclosure sales "are where buyers are going to get good deals on real estate."¹²⁹ And in many areas OREO¹³⁰ sales make up most of the market.¹³¹

Senate Bill 346 is the result of the committee's study and suggestions.¹³² The entire bill is comprised of twelve sections addressing multiple issues. The sections of the bill discussed below resolve the efficiency problems that led to over assessment for tax purposes despite the housing market decline.¹³³

Section five primarily deals with the use of terminology and definitions that govern county appraisal practices. It also instructs

Id. at 8. Therefore, despite the moratorium, about eighty counties reported increased tax digests. *Id.* at 8-9. And even without the exemptions to the moratorium, counties can still increase their revenues by raising the millage rates. *Id.* A reported thirty-six counties increased their millage rate in 2009 after the moratorium went into effect. So, even though values were frozen, property taxes still increased. *Id.*

¹²⁶ See Ga. S. Res. 685.

¹²⁷ PROP. TAX ASSESSMENTS & APPEALS STUDY COMM., FINAL REP., S. 150, Reg. Sess., at 9 (Ga. 2009).

¹²⁸ *Id.*

¹²⁹ *Id.*

¹³⁰ OREO stands for Other Real Estate Owned.

¹³¹ *Id.*

¹³² S. 346, 150th Gen. Assemb., Reg. Sess. (Ga. 2010).

¹³³ *Id.* at 1. Some other important aspects of the Bill are: eliminating the requirement that property owners submit a real property return in order to guarantee their right to appeal and establishing hearing officers to hear taxpayer appeals. Ga. S. 346.

county appraisers on how to resolve some of the discrepancy between assessments and falling home values.¹³⁴ First, it adds a new definition of an arm's length bona fide sale to section 48-5-2 of the Georgia Code.

'Arm's length, bona fide sale' means a transaction which has occurred in good faith without fraud or deceit carried out by unrelated or unaffiliated parties, as by a willing buyer and a willing seller, each acting in his or her own self-interest, including but not limited to a distress sale, short sale, bank sale or sale at public auction.¹³⁵

Secondly, Section five adds additional language to the definition of fair market value, requiring the consideration of the income approach when valuing a property.¹³⁶ It states: "[t]he income approach, if date is available shall be considered in determining the fair market value of income-producing property."¹³⁷ Next, this section also requires that a sales price "of the most recent arm's length, bona fide sale in any year" be the maximum taxable-value for the next year.¹³⁸ Finally, this section further directs appraisers to include non-traditional bank sales.¹³⁹ The word "consider" has been replaced with "apply" in section 48-5-2 of the Georgia Code.¹⁴⁰ Now county appraisers must apply bank sales when computing the fair market value using the sales comparable approach.

B. Reform in Florida

In 2007, Floridians were experiencing a housing and tax market similar to that of California in the 1970s before Proposition 13.¹⁴¹ As property values increased, local governments experienced as much as eighty-two percent increases in

¹³⁴ Ga. S. 346.

¹³⁵ Ga. S. 346 (codified as amended at GA. CODE ANN. § 48-5-2 (2010)).

¹³⁶ *Id.*

¹³⁷ *Id.*

¹³⁸ *Id.*

¹³⁹ *Id.*

¹⁴⁰ GA. CODE ANN. § 48-5-2 (2010).

¹⁴¹ See Padgett & Peltier, *supra* note 1; see also *supra* notes 48-53 and accompanying text.

revenue.¹⁴² This situation prompted the legislature to begin reforming the property tax system in Florida.¹⁴³ Florida's property tax reform has three important aspects: (1) the homestead exemption, (2) assessment caps, and (3) millage rate caps. The following sections discuss these three aspects.

1. The Homestead Exemption Provides Substantial Tax Breaks to Florida Homeowners

The Florida homestead exemption reduces tax liability by subtracting a certain dollar amount from a home's fair market value.¹⁴⁴ In order to qualify, one must be the owner of residential property in Florida and maintain that property as one's only permanent residence.¹⁴⁵

Every person who owns and resides on real property in Florida on January 1, and makes the property his or her permanent residence, may receive a property tax exemption up to \$50,000. The first \$25,000 applies to all property taxes. The added \$25,000 applies to assessed value over \$50,000 and only to non-school taxes.¹⁴⁶

Elderly homeowners over the age of sixty-five with annual income less than \$20,000 qualify for an additional \$50,000 subtraction from the fair market value of their property.¹⁴⁷ And there are additional exemptions for the disabled, widows, and veterans.¹⁴⁸

In 2007, the legislature increased the homestead exemption to seventy-five percent of the first \$200,000 in taxable (fair market) value with a minimum exemption of \$50,000 or \$100,000

¹⁴² Padgett & Peltier, *supra* note 1.

¹⁴³ *Id.*

¹⁴⁴ Melnik & Cenedella, *supra* note 2, at 278 ("Homestead exemptions exempt a certain portion of a residential home's value from taxation.").

¹⁴⁵ FLA. CONST. art. VII, § 6(a) (2010); *see also* FLA. STAT. ANN. § 196.031(1)(a) (West 2011).

¹⁴⁶ FLA. DEP'T OF REVENUE, EXEMPTION AND DISCOUNT REQUIREMENTS, *available at* <http://dor.myflorida.com/dor/property/taxpayers/pdf/hxexemptions.pdf> (last visited Apr. 20, 2012).

¹⁴⁷ FLA. STAT. §196.075(2) (Supp. 2011).

¹⁴⁸ *See* EXEMPTION AND DISCOUNT REQUIREMENTS, *supra* note 146.

for low-income seniors.¹⁴⁹ Beginning in 2008, homeowners were allowed to transfer their homestead savings when they move to a more expensive home.¹⁵⁰ If a homeowner moves to a less expensive home the savings are transferred on a pro rata basis.¹⁵¹ But either way, transferred savings only apply up to \$500,000 in value.¹⁵²

Currently, first time Florida homebuyers do not qualify for the homestead exemption; they are taxed at full fair market value.¹⁵³ In 2011, constitutional amendments were approved by the legislature and are up for public adoption in 2012. These amendments will make the homestead exemption available to first time homebuyers for twenty-five percent of the value of the home up to \$100,000.¹⁵⁴

2. Assessment Caps Insulate Taxpayers from Rapid Increases in Real Estate Values

Property owners also receive tax savings through Florida's cap on assessment increases. In any tax year a home's value can only increase by either three percent or the consumer price index of the preceding year, whichever is lower.¹⁵⁵ The Florida Department of Revenue explains:

Beginning the year after you receive [the] homestead exemption, the assessment on your home cannot increase by more than the lesser of the change in the Consumer Price Index or [three percent] each year, no matter how much the fair market value increases. If you have moved from one Florida homestead to another within the last two

¹⁴⁹ SEC'Y OF THE S., 2007-B SPEC. SESS., SUMMARY OF LEGISLATION PASSED, at 1 (revised June 20, 2007), available at <http://archive.flsenate.gov/Publications/2007B/Senate/reports/summaries/pdf/sessum07B.pdf>.

¹⁵⁰ *Id.*

¹⁵¹ See EXEMPTION AND DISCOUNT REQUIREMENTS, *supra* note 146; H.J. Res. 381, 22d Leg., 1st Reg. Sess. (Fla. 2011).

¹⁵² Fla. H.J. Res. 381.

¹⁵³ *Id.* at 1.

¹⁵⁴ Fla. H.J. Res. 381. It is projected that this amendment will reduce county revenues by: \$13 million in 2011, \$28 million in 2012, \$44 million in 2013, \$49 million in 2014, and \$51 million in 2015. *Id.*

¹⁵⁵ FLA. STAT. ANN. § 193.155 (West 2011).

years, you may be eligible to take some of your SOH savings with you.¹⁵⁶

Since 2009, commercial property assessments have also been limited to an increase of ten percent per year with the exception of school taxes.¹⁵⁷ These limits do not transfer to a new owner of the property. So a change in ownership triggers reassessment at fair market value.¹⁵⁸ Appraisers are still required to physically inspect and revalue all property every five years.¹⁵⁹ It is important to note that unlike Nevada, Florida's caps apply to increases in value, not the total bottom line tax bill.¹⁶⁰

3. Millage Rate Caps Insulate Taxpayers by Limiting Increases in Local Government Revenue to Population Growth

For tax year 2007-2008, local governments were required to roll back their property tax revenue by three percent, five percent, seven percent, or nine percent depending on the per capita increase in population they experienced over the past five years.¹⁶¹ The legislature also limited the growth of future revenue.¹⁶² "The growth in revenue from property taxes assessed by taxing authorities is capped at a rate equal to the growth in Florida per capita personal income plus new construction, unless the governing board of the taxing authority overrides the cap with a super-majority, unanimous vote, or referendum."¹⁶³ Because property taxes are the major source of funding for local governments, it is very important to note that Florida's limitations

¹⁵⁶ See EXEMPTION AND DISCOUNT REQUIREMENTS, *supra* note 146 (SOH stands for Save Our Homes).

¹⁵⁷ FLA. STAT. ANN. §§ 193.1554, 193.1555 (West 2011).

¹⁵⁸ FLA. STAT. ANN. §§ 193.1555, 193.1556 (West 2011).

¹⁵⁹ FLA. STAT. ANN. § 193.023(2) (West 2011).

¹⁶⁰ See EXEMPTION AND DISCOUNT REQUIREMENTS, *supra* note 146.

¹⁶¹ SEC'Y OF THE S., 2007-B SPEC. SESS., SUMMARY OF LEGISLATION PASSED, at 2 (June, 20 2007), available at <http://archive.flsenate.gov/Publications/2007B/Senate/reports/summaries/pdf/sessum07B.pdf>.

¹⁶² *Id.*

¹⁶³ FLA. DEPT OF REVENUE, *Local Governments that Levy Taxes*, <http://dor.myflorida.com/dor/property/taxpayers/> (last visited May 1, 2011).

are tied to local income and growth and that they may be overridden.¹⁶⁴

Florida adopted what is known as the truth in millage requirements (TRIM) that local governments must comply with when adjusting the millage rate.¹⁶⁵ The Florida law requires:

Before adopting a budget and setting a millage (tax) rate, taxing authorities must hold public hearings and follow the statewide truth in millage (TRIM) requirements. These meetings are the best opportunity for property owners to comment on taxing authority budgets and millages. Taxing authorities advertise meetings in local newspapers and usually post notices on local government websites.¹⁶⁶

The TRIM requirements give taxpayers a valuable opportunity to object to millage rate changes before they are implemented.¹⁶⁷

IV. MARKET VALUATION REFORM INCREASES EFFICIENCY, PROVIDES INSULATION, & PRESERVES EQUALITY

Lack of efficiency and insulation from market volatility are the two largest criticisms of market valuation.¹⁶⁸ These problems led to the adoption of California and Nevada's non-market systems that sacrifice equal distribution of the tax burden. They also led to the reform in Georgia and Florida discussed in the previous section. Georgia and Florida creatively adapted their market valuation methods to address the efficiency and insulation problems without adopting non-market valuation methods. Georgia's reform primarily focuses on increasing efficiency and accuracy in market valuation. While Florida's reform addresses the need for taxpayer insulation from drastic market changes.

¹⁶⁴ Melnik & Cenedella, *supra* note 2, at 264-65. ("Modern day municipalities depend on property taxes to finance many important public services, such as police and fire departments, education systems, and transportation systems.")

¹⁶⁵ *See Local Governments that Levy Taxes, supra* note 163.

¹⁶⁶ *Id.*

¹⁶⁷ *See id.*

¹⁶⁸ *See supra* notes 39-50 and accompanying text.

*A. Incorporating Acquisition Valuation in Market Valuation
Reduces the Number of Individual Appraisals*

Georgia's Senate Bill 346 requires that a sales price "of the most recent arm's length, bona fide sale in any year" be the maximum taxable-value for the next year.¹⁶⁹ Setting value at the sales price for one tax year is a quick way to determine the fair market value of property. Because fair market value is the price a willing buyer and seller would agree upon in an arms-length transaction, the sales price is a reliable determination of fair market value. Therefore, the Georgia legislature has reduced the need for many appraisals.

Setting the fair market value at a property's sales price also increases the accuracy of the overall tax digest. The tax concept of uniformity requires "two properties with similar utility to be valued alike."¹⁷⁰ It "guarantees that all property owners in a county are treated alike and ensures that the tax burden is spread across the spectrum as fairly as possible."¹⁷¹ By increasing efficiency, use of sales price data enables assessors to achieve uniformity because value data will be rapidly updated.

However, this could create a competitive advantage for commercial property owners in the first year. Reduced taxes could dramatically lower the cost of operating commercial property, increasing revenue and allowing the owner to charge lower rents. But for the rents to be significantly lower than the subject property's competitors the local taxing area would have to be highly over assessed. If the area is accurately valued then the new sales price should be in line with other similar valuations. So, the problems of a competitive advantage are only threatening in the event of outlier foreclosure sales or where assessments are extremely behind the market.

¹⁶⁹ S. 346, 150th Gen. Assemb., Reg. Sess. (Ga. 2010).

¹⁷⁰ PROP. TAX ASSESSMENTS & APPEALS STUDY COMM., FINAL REP., S. 150, Reg. Sess., at 9 (Ga. 2009).

¹⁷¹ *Id.* It was stressed that "uniformity protects the individual by balancing burdens on the assessor and the taxpayer." *Id.*

B. Including OREO Sale Data in the Computation of Fair Market Value Allows Appraisers to Quickly Capture Market Declines

Georgia's property reform also amends the definition of fair market value to include OREO sales.¹⁷² Changing appraisal practices to include OREO sales (transactions where a bank is the seller) increases the efficiency of market valuation. Including OREO data in the sales comparison approach quickly decreases data set values, creating lower valuations. Traditionally, OREO's were considered atypical non-arm's length transactions. Now, the increased number of foreclosures has increased OREO sales. Banks are able to offer very attractive prices because they only need to recoup the outstanding loan balance.

There are two important considerations when using OREO sales data. First, there is confusion about what constitutes an OREO sale. The term does not refer to the transaction in which a bank forecloses on property. An OREO sale is when, after foreclosing on the property, the bank sells to a third party. The foreclosure transaction is not arm's length because the bank has an interest in the property.

The second consideration is whether a legislature should require assessors to consider or apply OREO sales in valuations. The Georgia legislature changed the OREO sale provision from "consider" to "apply" when using the transactions.¹⁷³ However, there is a potential drawback to this requirement. Although the overall real estate market is in a downward trend, not all sub-markets experience high volumes of bank sales. In those markets the mandatory use of OREO sales actually requires the appraiser to include outliers.

¹⁷² See Ga. S. 346.

¹⁷³ Ga. S. 346. Senate Bill 346 provides that:

'Arm's length, bona fide sale' means a transaction which has occurred in good faith without fraud or deceit carried out by unrelated or unaffiliated parties, as by a willing buyer and a willing seller, each acting in his or her own self-interest, including but not limited to a distress sale, short sale, bank sale or sale at public auction.

GA. CODE ANN. § 48-5-2 (2010).

*C. Income Data Allows Assessors to Make Accurate Valuations
When Sales Data is not Available*

Requiring tax assessors to consider income data from income producing property increases the accuracy of valuations in Georgia.¹⁷⁴ The income approach allows tax assessors to accurately value property when sales data is scarce. In a declining market there may not be enough sales data for a true like-kind comparison under the sales comparison approach. In this situation, the income approach is more reliable because it bases a property's value on the revenue generated by the property.

One of the benefits of the income approach is that it is an accurate valuation method in periods of growth, decline, and stability. The income produced by a property will adjust to reflect a property's economic value. Therefore, it is a reliable source of information regardless of whether the economy is doing well or in a recession. However, it is more beneficial in a recession when the sales comparison approach becomes less reliable.

*D. Florida's Homestead Exemption is a Proportionate Reduction
of Tax Liability*

One major benefit of acquisition valuation is that property owners experience a comparative reduction in their tax liability as time passes.¹⁷⁵ The homestead exemption also reduces tax liability, but does so proportionate to value and ability to pay in the form of a reduction.

The exemption is proportionate because the reduction is applied as a percentage of the value of qualifying homes.¹⁷⁶ Further, the amount of one's homestead exemption varies based on age, income, and disability.¹⁷⁷ Therefore, Florida residents with the least ability to pay will receive the greatest reductions.

In addition to being proportionate, the homestead exemption has other benefits over the acquisition value "privilege." First,

¹⁷⁴ See Ga. S.B. 346.

¹⁷⁵ See CAL. STATE BD. OF EQUALIZATION, *supra* note 53 ("Longtime property owners, whose assessed values generally may not be increased more than 2 percent per year, tend to have markedly lower tax liability than recent purchasers, whose assessed values tend to approximate market levels.").

¹⁷⁶ See *supra* note 143 and accompanying text.

¹⁷⁷ See *supra* notes 144 -45 and accompanying text.

homes receiving an exemption are still reassessed to keep values current. Second, the homestead exemption applies regardless of fair market value so that taxpayers receive reductions in periods of both growth and decline. Finally, Florida allows homeowners to transfer their savings to new home purchases so that tax liability does not discourage moving.

One drawback of homestead exemption programs is that they may cause a shift in tax burdens from one taxpayer to another:

Because localities depend heavily on the property tax for revenue, the likelihood is that the locality will raise property tax rates to make up for exemption-driven losses in tax revenues. In states in which not all property qualifies for the exemption, the increase rates will disproportionately burden properties that do not qualify for the homestead exemption. This is because the higher tax rate will apply to the entire value of a property that does not qualify for the homestead exemption.¹⁷⁸

However, Florida avoids shifting the burden by increasing the availability of the homestead exemption, making the homestead exemption portable, providing assessment caps to commercial properties that do not qualify for the exemption, and most importantly by capping millage rate increases.

E. Assessment Caps Insulate Taxpayers from Market Volatility Without Creating a Privilege for Long-Term Property Owners or Commercial Property

Assessments in Florida are limited to an increase of three percent per year for residential property and ten percent per year for commercial.¹⁷⁹ Initially, it appears that Florida's cap will have the same effects on equality as acquisition valuation, which only allows assessments to increase by two percent per year.¹⁸⁰ However, there are subtle but important differences in how these two limitations on assessment increases affect taxation.

¹⁷⁸ Melnik & Cenedella, *supra* note 2, at 280.

¹⁷⁹ FLA. STAT. ANN. § 193.1555 (West 2011).

¹⁸⁰ See *supra* note 76 and accompanying text.

First, Florida does not use the same assessment cap for commercial and residential property.¹⁸¹ This allows commercial property to carry a larger percentage of the tax burden unlike acquisition valuation.¹⁸² Recall that under acquisition value there is no discernment between land use for taxation purposes. The only qualifier is the property's purchase date. Since commercial property generally has a lower turnover rate than residential, it remains locked in at an older purchase price and therefore lower valuation and tax burden.¹⁸³ Florida avoids this problem by capping assessments for residential at three percent increases per year and non-residential at ten percent per year.

Second, the cap in Florida only limits increases in the assessment, not whether property values can be changed.¹⁸⁴ Property values can be reduced in a recession. This avoids another problematic aspect of acquisition valuation that is especially relevant today. California property tax valuations do not automatically decrease when the market decreases. Because the value is only reset upon a change in ownership, many properties purchased during the bubble are now overvalued. This causes a reverse "privilege" as discussed previously.¹⁸⁵

Finally, the assessment cap implemented in Florida actually limits property taxes unlike Nevada's cap on the total tax bill. In Florida, the cap only applies to the value part of the tax equation, not the total amount due on the tax bill.¹⁸⁶ When the value decreases, the tax bill must also decrease. Recall that by capping the total amount, Nevada's caps actually allowed the total tax to increase despite a decrease in the property's value.¹⁸⁷

F. Limitations on Millage Rate Increases Prevent Local Government Windfalls

Caps on millage rate increases alleviate another aspect of market valuation that led to the adoption of Proposition 13 and

¹⁸¹ See § 193.1555.

¹⁸² See *supra* notes 82-87 and accompanying text.

¹⁸³ See *id.*

¹⁸⁴ See § 193.1555.

¹⁸⁵ See *supra* notes 101-104 and accompanying text.

¹⁸⁶ See § 193.1555.

¹⁸⁷ See *supra* notes 108 and accompanying table.

taxable-value. The caps prevent local governments from simply increasing the millage rate when the tax digest decreases. Limiting the millage rate to the rate of population growth in a taxing jurisdiction keeps the tax revenues in line with local government expansion, not real estate market changes.

Florida is not the first state to implement a millage rate cap.¹⁸⁸ However, other states implementing similar caps have found that they do not actually reduce property taxes. Recall that “the tax rate is only one of two factors used to determine the amount of taxes due; assessed value is the other factor. Therefore, a homeowner in an area with rising assessment values will nevertheless experience rising property tax bills even though the tax rate is kept constant.”¹⁸⁹ Florida’s millage rate cap, however, is implemented in conjunction with an assessment cap. The two caps work together to prevent the taxing jurisdiction from circumventing either limitation.

CONCLUSION

California, Florida, Georgia, and Nevada have all implemented legislation to limit the amount property taxes can increase during a rapidly rising housing market. The early 2000 housing bubble and following real estate recession have prompted many state legislatures to reform their property tax methods. These dramatic fluctuations in the real estate market have generated support for abandoning the traditional market based method of property valuation. However, California and Nevada demonstrate that non-market property taxation is not equitable and can be difficult to implement. In response to the housing bubble and recession, the Georgia and Florida legislatures reformed their market based taxation systems. Taken together, market valuation in these two states preserves equity and achieves the goals of non-market taxation: increased efficiency, accuracy, and insulation from market volatility.

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¹⁸⁸ Melnik & Cenedella, *supra* note 2, at 286.

¹⁸⁹ *Id.* at 287.