A report submitted to the Minnesota State Legislature

pursuant to

Minnesota Statutes, section 270C.991, subdivision 4

Property Tax Working Group
November 30, 2012

www.revenue.state.mn.us/propertytax/pages/workgroup

Executive Letter

November 30, 2012

Sen. Rod Skoe
Chair-elect, Senate Committee on Taxes
Capitol Building
75 Rev. Dr. Martin Luther King Jr. Blvd.
St. Paul, MN 55155

Rep. Ann Lenczewski
Chair-elect, House Taxes Committee
State Office Building
100 Rev. Dr. Martin Luther King Jr. Blvd.
St. Paul, MN 55155

Dear Sen. Skoe and Rep. Lenczewski,

I am pleased to present to you the findings and recommendations of the Property Tax Working Group.

The 2010 Legislature established the Property Tax Working Group to explore the unique complexities of Minnesota's property tax sy dations set forth in this report. The Working Group, consisting of volunteer members appointed by various stakeholder organizations, including the Legislature, and two homeowners appointed by the Commissioner of Revenue, has met and deliberated for two years to develop these recommendations. I want to specially acknowledge the work and expertise of Stephen Behrenbrinker and Luayn Murphy, who served as subcommittee chairs and the assistance of Jason Nord and Jessica Harding from the Minnesota Department of Revenue, who served as staff for the Working Group.

While the challenge we faced in addressing the complexities of the Minnesota property tax resulted in differing viewpoints, this report represents the consensus of the group. We believe this report will be useful for years to come in identifying principles, goals, and direction that will lead toward a more transparent, understandable, simple, efficient, equitable, stable, predictable, accountable, competitive, and responsive property tax system.

We appreciate the opportunity to help begin the process of simplifying and improving the Minnesota property tax system and encourage the Minnesota Legislature to address property tax simplification as part of its tax reform efforts.

Sincerely,

Kathleen A. Gaylord
Chair

Per Minnesota Statutes, section 3.197, any report to the legislature must contain, at the beginning of the report, the cost of preparing the report, including any costs incurred by another agency or another level of government.

This report cost $41,000.

Membership

Kathleen A. Gaylord (Chair)
Dakota County Commissioner
Association of Minnesota Counties

Rep. Denise Dittrich
Minnesota House of Representatives

Rep. Greg Davids
Minnesota House of Representatives

Sen. Rod Skoe
Minnesota Senate

Sen. Warren Limmer
Minnesota Senate

R. Thomas Mould
Homeowner (under age 65)
Minnesota Department of Revenue

Eric Sorensen
Homeowner (age 65 or older)
Minnesota Department of Revenue

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Matt Van Slooten
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Minnesota Chamber of Commerce

Stephen Behrenbrinker
Assessor, City of St. Cloud
Minnesota Association of Assessing Officers

Chris Radatz
Public Policy Director,
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Minnesota Farm Bureau and Minnesota Farmers Union (Joint Appointment)

Alternates* & Former Members†

- Rep. Linda Runbeck,* *Minnesota House of Representatives*
- Sen. Rick Olseen,† *Minnesota Senate*
- Jason Nord,† *Minnesota Department of Revenue*
- Cal Larson,† *Homeowner age 65 or older, Minnesota Department of Revenue*
- David Fricke† and Gary Pedersen,* *Minnesota Association of Townships*
- Craig Patterson* and Doug Fulton,* *Minnesota Chamber of Commerce*
- Bill Effertz,* *Minnesota Association of Assessing Officers*
- Thom Petersen,† Government Relations Director, Minnesota Farmers Union, *Minnesota Farm Bureau and Minnesota Farmers Union (Joint Appointment)*

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Executive Summary

The Property Tax Working Group was created in 2010 to examine the many facets of Minnesota's property tax system and develop recommendations on how to make the system more simple, understandable, transparent, accountable, and efficient. The Working Group held 20 meetings from October 2010 through November 2012.

The following summary of Guiding Principles and Recommendations established by the Property Tax Working Group are the result of two years of extensive research and debate. Full details of the principles and recommendations are provided in the full report.

Guiding Principles

- **Defend the purpose**
  The purpose of the property tax is to provide local revenue to pay for local services. The property tax is not a vehicle for state policies. The state's involvement s

- **Base property taxes on market value (true ad valorem system)**
  Property taxes should always be based on full estimated market value to minimize confusion, complexity, costs, and distortions.

- **Base property taxes on property attributes, not ownership or occupancy**
  The characteristics and use of a property should drive property tax levels, while the characteristics of an owner or occupant should be delivered via the income tax system.

- **Defend broad-based goals from narrow interests**
  Creating new classifications or benefits for individual or narrow subgroups of property should be avoided to preserve transparency, simplicity, and efficiency in the system. The cost of administering narrow preferences often outweighs the benefits received.

- **Consider more transparent alternatives**
  When evaluating new property tax proposals, legislators should consider whether the special provision is needed and if there are other ways to deliver the benefit outside the property tax system. The property tax should not be used simply to avoid direct state costs.

- **Provide sunsets to prompt review**
  Any new changes in the property tax system should have a sunset date to force reevaluation over time and remove provisions that are no longer achieving their intended goals.

- **Require value or intention statements on new legislation**
  New property tax proposals should include a statement that describes why the change is necessary and valuable, what it intends to do, and what alternatives were considered. This will enrich reevaluation and decision-making when the provision is set to expire.

- **Make simplicity and transparency a priority**
  A transparent and understandable system facilitates trust and accountability. A simple system is more efficient and reduces errors, unintended outcomes, and high costs. Policymakers must defend these important principles.

- **Require local impact notes for any property tax changes**
  Local impact notes should be required for all proposed changes to the property tax system to increase accountability.

Our Recommendations

1. **Reduce the number of classifications**
   Consolidate the number of classifications from 15 to 4 (residential, agricultural, commercial, other). Do not target benefits to specific properties through micro classification.

2. **Homestead benefits—Expand the Property Tax Refund (PTR) program**
   Expand the Property Tax Refund program as the primary method of homestead benefit. Standardize the definition of a homestead for both residential and agricultural properties.

3. **Avoid or eliminate tiers and parcel linkage**
   Eliminate value tiers to avoid needing to chain parcels based on ownership, thereby reducing confusion, complexity, and administrative costs.

4. **Revamp the agricultural homestead classification process**
   Enact *Recommendations 1-3* (condense classifications, standardize the homestead definition, eliminate tiers/parcel linkage) to greatly simplify the agricultural homestead process.

5. Establish an agreed upon relationship (ratio) between classification rates

Do not use classification rates to provide benefits to narrow groups. Establish and maintain consistent ratios; recognize that ratio changes shift burdens to other properties.

6. Consolidate reporting, application, and effective dates

Consolidate the property tax calendar around a few key dates to increase understandability, predictability, and compliance.

7. Base assessments on the most current economic conditions

Support recent sales analysis efforts that make the system more responsive. Encourage the transition to eCRV. Use a larger geographic area for sales comparisons.

8. Make improvements to the Truth in Taxation (TNT) process

Show basic budget information or provide links on TNT notices and direct the public to websites with more detailed information. Modernize the process and engage taxpayers electronically.

9. Make improvements to notices and statements

Give notices consistent branding and distribute electronically. Include websites and email contacts. Improve timing and coordination. Show estimated and taxable market values.

10. Investigate and plan for an eventual statewide computer system

Explore the creation of a centralized tax system to support local administration of the tax, save total state and local costs, and improve accountability.

11. Convert the tax capacity system to an assessed value system

Use assessed values and mill rates to make ... standable, transparent, and competitive across the nation.

12. Eliminate the use of property taxes for state funding

Eliminate the state tax to restore property taxes as a local tax and reduce complexity. If not eliminated, designate revenues directly for local governments, not the general fund.

13. Avoid limits, caps, and freezes

Do not impose limits, caps, or freezes on values, tax amounts or levies. This undermines budgeting and causes inequities. Let local governments be accountable to local voters.

14. Exclusions

The state should not use exclusions to avoid paying for benefits it thinks are important, nor for short-term or one-time benefits. If used, tie exclusions to properties, not owners. See full report for recommendations on specific exclusions.

15. Credits

Eliminate/phase out power line credit (high admin costs) and agricultural homestead credit (result of other recommendations). Keep disaster and disparity reduction credits.

16. Exemptions

Be selective—exemptions must accomplish public purposes, not serve special interests. Impose automatic review/sunset dates to improve accountability and verify success. See full report for recommendations on specific exemptions.

17. Aids

Allow Utility Valuation Transition Aid to naturally phase out. Sunset or phase-out Disparity Reduction Aid (1988 legacy aid, may no longer achieve intended goals).

18. Special Valuations and Deferrals

These programs increase complexity and decrease efficiency, transparency, and accountability. Impose sunset dates on all current/future programs to prompt review.

19. Refunds

Expand the homeowner Property Tax Refund (PTR) program. Keep special targeting PTR as a tool to ease impacts of other reforms. Reevaluate renter PTR with respect to class consolidations in *Recommendation 1*.

A downloadable copy of this report, along with meeting materials, research, and other information related to the Working Group can be found online at:

www.revenue.state.mn.us/propertytax/pages/workgroup

Introduction

Background

The Property Tax Working Group was established during the 2010 legislative session as one component of a broader statute (M.S. § 270C.991) enacted to address property tax system accountability and evaluation. The express purpose behind these measures was to provide state policy makers with the tools to create a more accountable and efficient property tax system.

Goals of the Property Tax Working Group

The statutory goals of the Working Group are:[1]

(1) to investigate ways to simplify the property tax system and make advisory recommendations on ways to make the system more understandable;

(2) to reexamine the property tax calendar to determine what changes could be made to shorten the two-year cycle from assessment through property tax collection; and

(3) to determine the cost versus the benefits of the various property tax components, including property classifications, credits, aids, exclusions, exemptions, and abatements, and to suggest ways to achieve some of the goals in simpler and more cost-efficient ways.

Tax Principles

The statute also laid out several basic property tax principles that should be taken into consideration in evaluating property tax proposals that come before the legislature.[2] The proposed outcomes should be:

(1) transparent and understandable;
(2) simple and efficient;
(3) equitable;
(4) stable and predictable;
(5) [conducive to] compliance and accountability;
(6) competitive, both nationally and globally; and
(7) responsive to economic conditions.

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[1] Minnesota Statutes, sec. 270C.991, subd. 4.
[2] Minnesota Statutes, sec. 270C.991, subd. 2.

Meetings and Activities

The Property Tax Working Group held numerous meetings from 2010-2012 to evaluate and consider the wide array of complexities and features of Minnesota's property ta The Working Group also formed a pair of subcommittees to hold more detailed discussions of classification and agricultural issues. Meetings and their topics were held as follows:

Oct. 7, 2010

- First meeting, chaired by the Minnesota Department of Revenue
- Welcome and Introductions
- Review of the Group's Charge
- *Property Taxes & Complexity* – Presentation by Jason Nord, Minnesota Department of Revenue
- Election of Chair
- Discussion

Nov. 18, 2010

- *Legislative Origins of Minnesota's Property Tax Working Group* – Presentation by Katherine Schill, House Fiscal Analysis
- *Property Tax Principles, Indicators and Inventory* – Presentation by Eric Willette, Minnesota Department of Revenue
- Property Tax Inventory Report
- Work plan discussion

Dec. 9, 2010

- Members' Lists of Priorities for the Property Tax Working Group
- Discussion of ways to prioritize

Jan 14, 2011

- Background information on the classification system
- Discussion of the classification system

Feb. 11, 2011

- Discussion of the classification system
- Review of requested alternatives for residential and seasonal business property
- Classification subcommittee formed

March 11, 2011

- *Minnesota's Agricultural and Rural Land Classifications: The Assessment of Agricultural Land and Rural Vacant Land* - Presentation by Michael Stalberger, Minnesota Department of Revenue and Jeanne Henderson, Sherburne County's Office / Minnesota Association of Assessing Officers (MAAO) Agricultural Committee Chair
- Chaining/ownership example – Tom Dybing, Houston County Assessor
- Discussion of agricultural classifications and homesteads

April 8, 2011

- Classification subcommittee update
- Letter regarding agricultural classification input from MAAO
- Review of requested agricultural model run
- Agricultural subcommittee formed

June 15, 2011

- Classification subcommittee update
- Discussion of classification
- Introduction to property tax calendar
- Discussion of the property tax calendar

Aug. 17, 2011

- Legislative changes to the Working Group
- 2011 property tax system law changes
- Exclusions and credits
- Property classifications by state
- Discussion of work strategy

Sept 21, 2011

- Classification subcommittee update
- Minnesota property tax refund history
- Summary of tax bases
- Exclusions in other states

Nov. 16, 2011

- Agricultural subcommittee update
- Review of requested agricultural demo run
- Classification subcommittee update
- Review of requested full class model run
- Discussion of valuation notices, truth in taxation notices, and property tax statements
- Review of consensus points and preliminary draft recommendations
- Discussion

Jan 18, 2012

- Consensus points and preliminary draft recommendations, review changes made at November meeting
- Discussion of property tax calendar
- Discussion of statements and notices
- Discussion of exclusions, credits, and exemptions

Feb. 15, 2012

- Consensus points and preliminary draft recommendations, review changes made at January meeting
- Update on property tax calendar
- Discussion of exclusions, credits, and exemptions

March 23, 2012

- Property Tax “work” Benefits through and discussion of items

June 20, 2012

- Consensus points and preliminary draft recommendations, review updates, work through items

July 18, 2012

- Consensus points and preliminary draft recommendations, review updates, work through items

Aug. 15, 2012

- Updates from Other Property Tax Study Groups
- *Local Government Aid (LGA) Study Group*—Presentation by Pat Dalton, House Research
- *PILT Report Commissioner's Advisory Group*—Presentation by Susan Damon, Minnesota Department of Natural Resources
- *Alternative Methods of Valuing Agricultural and Rural Vacant Land*—Presentation by Andrea Fish, Minnesota Department of Revenue
- Consensus points and preliminary draft recommendations, review updates, work through items

Sept. 19, 2012

- Updates from other Property Tax Study Groups
- *Governor's Tax Reform for a Better Minnesota*—Presentation by Susan Von Mosch, Minnesota Department of Revenue
- Review of draft report.
- Revisit classification and homestead recommendations, and other items needing further review.

Oct. 17, 2012

- Review and discussion of draft report.

Nov. 14, 2012

- Finalize report.

Classification Subcommittee Meetings

- March 28, 2011
  Discussed "Hot House" model runs and ranked scenarios. Briefly discussed going to four classes and the differences between state and local class rates. Discussed consolidating smaller classifications.
- June 7, 2011
  Reviewed previous discussions. Discussed approaches
- Sept 8, 2011
  Finalized recommendations on consolidation of the classification system to bring to full Working Group.

Agricultural Subcommittee Meetings

- June 15, 2011
  Reviewed previous discussions from full Working Group. Discussed approaches
- Sept 21, 2011
  Reviewed purpose of subcommittee. Discussed homestead linkages and benefits; HGA; ownership entities; valuation tiers, borrowing, credits, and exclusions based on use vs. ownership; properties subject to referendums; single class rate. Reviewed April 8 recommendations from MAAO.

Property Taxes in Minnesota

History

Property Tax's Pioneering Role

Minnesota and large portions of North and South Dakota were organized into the Territory of Minnesota by the Organic Act of 1849. That year—nine years before Minnesota became a state—the first territorial assembly established a property tax levy to fund schools. The levy was equal to "one fourth of one percent on the ad valorem amount of the assessment rolls made by the county."[3] Property taxes would remain the main source of state revenue until motor vehicle registration and gasoline taxes were adopted in the 1920s, with individual and corporate income taxes not arriving until 1933.

In becoming a state, Minnesota's constitution provided that taxes should be equalized and uniform. It also provided exemption from taxation for:

- public burying grounds;
- public school houses;
- public hospitals;
- academies, colleges, universities, and all seminaries of learning;
- all churches, church property used for religious purposes, and houses of worship;
- institutions of purely public charity;
- public property used exclusively for any public purpose; and
- personal property to an amount not exceeding in value two hundred dollars for each individual.

Difficulties in assessment procedure and inexperienced assessors led to the creation of the State Board of Equalization in 1860. To compensate for shortfalls caused by undervaluations and assessment inequities, Governor Ramsey cut the salaries of state officials, reduced the size of the legislature and submitted a constitutional amendment to cut the length of legislative sessions as a means to cut state expenses by 36 percent.[4] Uniform assessment, ever an important principle, was a major goal throughout the late 1800s.[5]

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[3] Laws of Minnesota 1849, ch. 7, sec. 2.
[4] Kathleen A. Gaylord and Susan Chianelli Jacobson, *History of Taxation in Minnesota* (Tax Study Commission, 1979), 11.
[5] Ibid., 12.

Uniformity and Classification

In 1905 the Legislature proposed a constitutional amendment referred to as the "wide op amendment. Adopted by voters in 1906, the amendment removed many of the restrictions on the legislature's power of taxation, and mains today) that "taxes shall[6] This language re uniform o placed the restriction that "all taxes...shall b "equal and uniform throughout the state."[7]

This allowance for uniformity within classes, as opposed to stricter uniformity without classification, paved the way for a formal property tax classification system with separate classification ratios for each class. Such a classification system was first established in 1913 when the Legislature created four classes of property:

Class	Description	Ratio
1	Iron Ore Mined or Unmined	50%
2	Household Goods and Personal Effects	25%
3	Unplatted Real Estate; Livestock, Farm Produce, Inventories; and Manufacturers	33⅓%
4	All Other Property (primarily Urban Real Estate)	40%

The Great Depression brought massive delinquencies and a demand for property tax relief. Therefore, in 1933, the Legislature not only enacted income taxes as a major new source of revenue, it also enacted the three new classifications under the property tax system:

Class	Description	Tier	Ratio
3a	Agricultural Machinery and Horses Used by The Owne and Agricultural Products in the Hands of the Produce	--	10%
3b	Unplatted Real Estate Used for a Homestead	First $4,000 Excess	20% 33⅓%
3c	Platted Real Estate Used for a Homestead	First $4,000 Excess	25% 40%

These changes brought with them the concept of homestead benefits and the concept of value-based tiers within a classification.

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[6] Minnesota Constitution, art. 10, sec. 1.
[7] Gaylord and Jacobson, 12.

Evolution of the Formal Classification System

The 1933 changes were the first of many change… classifications have been changed in virtually every session dating back to 1941. Appendix B offers a summary of the evolution of the classification system, looking at six points in time (1913, 1933, 1953, 1973, 1993, and 2011).

Generally, from 1933 and into the 1970s, new classifications were carved out from broader classes, and some of the terminology evolved (e.g., from “unplatted” to “rural” to “agr… tural”), existing classification ratios were not altered. This started to change in the 1970s when the existing ratios began to be adjusted in addition to the proliferation of new classifications.

Classifications have bee… changed in virtually … session dating back to…

In 1985, the Legislature recodified the classifications into their current major groupings and organization. The class rates also changed significantly in their terminology and nominal expression when the major shift occurred from the old “assessed value … capacity and tax rates”. For example, the first tier of residential homesteads went from a *ratio* of *17%* for taxes payable in 1988 to a *class rate* of *1.00%* for taxes payable in 1990.

In the late 1990s and first couple years of the new millennium, class rate compression became a focus as the spread between the higher rates on commercial/industrial property and the lower tier of homestead property was seen as too disparate.

In recent years, numerous smaller classifications have been added that generally encompass a limited number of properties. Although the classifications can be counted in many ways (by major label, by tiers, by distinct rates), the number of distinctly described classifications is as high as 55 as of taxes payable in 2012.

Property Taxes Go Local

The shift toward the income tax (and other state taxes) and away from the property tax as the major source of state revenue primarily evolved from the 1920s to the 1960s. The property tax decreased from 50% of state tax revenue in 1903 to 6% in 1962, but accounted for 97% of local tax collections in the early 1960s.[8] In 1967, the state property tax was eliminated and collection of property taxes was turned over to the counties. That same year, the state instituted the sales tax, in part to offset the loss in revenue it experienced by turning property taxes over to local governments, but also to generate money for property tax relief.

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[8] Ibid., 39.

Relief in the 1960s

The 1967 *Tax Reform and Relief Act* marked a turning point in the state taking on a significant role in providing direct property tax relief and in establishing a state and local fiscal relationship of aid going to local governments as a means to lighten property tax burdens. The state created the Property Tax Reli[ef] Fund from the new sales and use tax, an increase in the corporate income tax, and other sources. The Act also established six programs:

- Homestead Property Tax Credit (property taxes reduced 35% up to $250)
- Renter Income Tax Credit (for a portion of rent paid)
- Senior Citizen Income Tax Credit (for property taxes paid up to $300)
- Personal Property Exemptions (relief funds reimbursed taxing districts for lost tax base)
- Elimination of the State Mill Levy (relief funds were used to reduce the mill levy for retirement costs)
- Local Government Aids (direct funds to schools and local governments)

Within the scale of these major changes it might [be] easy to overlook that the Green Acres program (Minnesota Agricultural Property Tax Law) was created in 1967 (it would not garner much further attention for almost 40 years). In 1969, the Open Space Property Tax Law was established. These deferral programs reduce the value on which qualifying lan[d] are taxed, "defer ... until the ... backs" time the land leaves the program. These programs and the advent of the Taconite Homestead Credit in 1969, however, were largely footnotes in this per[iod] of examining larger analysis of overall property tax burdens.

- **1913** – Classification system enacted with four classes
- **1933** – Number of property classes increase to seven
- **1937** – Homesteads get $4,000 exemption from state tax
- **1967** – State levy eliminated; Renter, senior, & homestead credits created; LGA, Green Acres created
- **1971** – Levy limits and Metropolitan Fiscal Disparities enacted
- **1975** – Property Tax Refund (Circuit Breaker) created
- **1982** – Reduced assessments for property damaged by a natural disaster enacted
- **1983** – Classification ratios changed; New PTR formula; 240-acre limit for farm homesteads removed
- **1987** – Number of classes reduced, ratios increased; Native Prairie and Wetlands Credits repealed
- **1988** – Truth-in-Taxation created; Ratios and mill rates replaced by tax capacity system

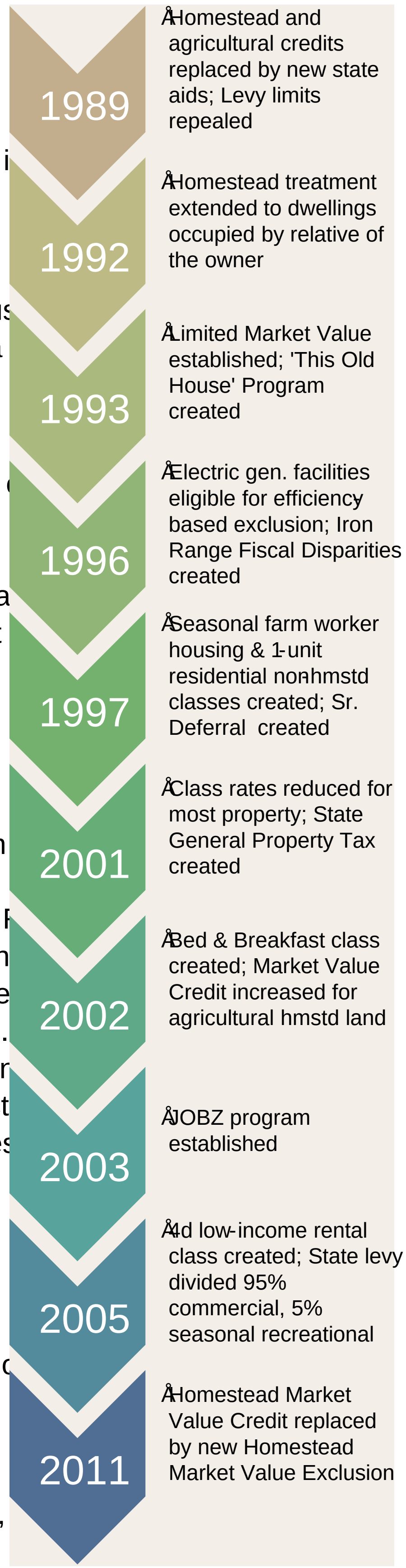
Property taxes were significantly reduced by the 1967 changes but continued to increase substantially in the following years, focused on relief. In 1971, the Legislature responded with levy limitations on all units of government in an effort to restrain the growth in property taxes. In addition, the 1971 Legislature created the Fiscal Disparities program as a means of tax base sharing in the metropolitan area. The value basis for property taxes was also changed from an adjusted market value (generally a third of the full market value), to use the full market value. This move tripled values, but cut mill rates by a comparable scale.

Relief continued in 1973 with a first incarnation of limited market value that limited assessment increases, and with the provision of a Senior Citizen Property Tax Freeze. The limited market value program was significantly changed in 1975, and a 1979 Tax Court ruling prompted further changes and a phase out when it found its previous structure to be unconstitutional. The senior freeze was replaced in the following years as new refund programs were developed.

In 1975, the Legislature enacted an adjusted homestead credit breaker further developed and renamed the Property Tax Refund in 1977. These programs for homeowners and renters provided state reimbursement of a share of the tax exceeding a percentage of household income. These programs would continue to see many changes over the years but maintain the same basic structure. The additional targeted refund for sharp increases in taxes arrived in 1980.

Changes Endure

From the late 1970s and into the late 1980s, the Legislature made frequent adjustments to classifications, the size of farm homesteads, and the structure of the homestead and agricultural credits. However, several new exemptions, credits, and programs came into being during this period, including: powerline credits,



wetlands exemptions and credits, native prairie exemptions and credits, and enterprise zones and credits. The wetland and native prairie credits would be short-lived and were repealed in 1987. This time period also saw the explosion of tax increment financing (TIF) which would trigger reforms and continual tinkering over the years.

A New Identity

1987-1989 brought more substantial changes. Possibly the largest single change occurred when the tax capacity system was introduced, replacing the assessed value and mill rate system. Taxes paid in 1989 served as a bridge, ut fore "net tax capacity" ... ng with taxes payable in 1990. ... minant This design is unique to Minnesota and the class rates were meant to identify appropriate levels of burden. The first tier of homesteads has ... had the benchmark class rate of 1.00% which serves as a measuring stick for other classes. (For example, commercial class rates have generally ranged from 2% to 5%, establishing easy to identify 2-to-1 or 5-to-1 relationships.) Tax rates were imagined to ideally center around 100%, making it easier to ... However, these rates, in nominal "high" o terms, often confuse observers from other states and seem shockingly high to those still accustomed to a mill rate system.

Other significant changes in the 1987-1989 sessions included repealing levy limits in favor of the "Truth in Taxation" (TNT) process, replacing homestead and agricultural credits with Homestead and Agricultural Credit Aid (HACA), and the creation of Disparity Reduction Aid (DRA). TNT is a formalized process for establishing proposed levies, notifying taxpayers, and holding hearings at which taxpayers can react before final levies are adopted. HACA was a grandfathered aid that would be used to help facilitate class rate compression in the following decade before its repeal. DRA was meant to ease the transition to the NTC system, but it remains today as a legacy aid.

The 1990s

Aside from the theme of class rate compression that began later in the decade, the 1990s mostly featured continual incremental changes. Some of the more notable changes include: the growth of homestead eligibilities, the creation and evolution of referendum market value as an alternate tax base, the return of lim... Old House", the creation of the Iron Range fiscal disparities program, the return of levy limits, the return of a homestead credit (as the education homestead credit), and the creation of the Senior Citizens Deferral program.

The Big Plan

The turn of the millennium brought some surpluses and a new governor. Governor Ventura made a push for policy and administrative reforms. The administrative component of this was a complexity tackling effort that perhaps got lost in the bigger policy discussion. The Big Plan yielded another substantial shift of the state taking over a significant share of school levies and redefining and increasing local government aids. The state general property tax levy was created, marking a return for property taxes as a state revenue source. The education homestead credit was replaced by new market value homestead credits for residential and agricultural properties that would increase and phase out according to property's, with reimbursement payments made to local governments.

> *The past several years have largely been marked by growing stress in state-local relationship, primarily caused by the frequent and large deficits. As the economy has suffered, so have state and local finances.*

Reactions to Fiscal Stress

The past several years in the wake of the Big Plan reform have largely been marked by growing stress in the state-local relationship, primarily caused by the frequent and large state deficits. As the economy has suffered, so have state and local finances. The state has made several cuts to local government aid and credit reimbursements. Pressures on property tax increases have been a source of frustration and the property tax refund program has been expanded. The 2011 session also included a replacement of the residential homestead market value credit with a new homestead exclusion, which has been the dominant issue of late.

The changing economy has also affected different classes of property in different ways. Agricultural property taxes have been a particular area of focus. Green Acres received a fair amount of attention, complete with newly defined agricultural and rural vacant land classifications.

Other notable changes over the past decade include the Job Opportunity Building Zone (JOBZ) program and its unique partial exemption, the transfer of wind energy systems from the property tax to a production tax, the elimination of limited market value, the creation of the Sustainable Forest Incentive Act (SFIA) program, and continued classification changes.

The Property Tax System Today: Complexity Abounds

Breadth of Complexity

Minnesota's property tax is a complex syste
in many different ways, including:

- aids to jurisdictions to reduce their property tax reliance,
- reductions in taxable value through exemptions and exclusions,
- differential weighting of taxable value through classification and multiple tax bases,
- reductions in final tax bills through credits, and
- refunds after taxes are paid.

The multitude of overlapping features and mechanisms is one trademark of property taxes in Minnesota. While taxpayers may expect that property taxes should be as simple as multiplying their property value by the tax rate, there are many less-than-transparent ways in which the value, rate, and tax are manipulated. A common misperception is that governments adopt tax rates, but they actually adopt levies (a dollar amount of taxes to be raised). The tax rates are the result of dividing the adopted levy by the tax base.

The vast array of features that manipulate levies, tax bases, and rates generates complexity and reduces efficiency and understandability, as illustrated in Figure 1.

Depth of Complexity

Another trademark of Minnesota's complexity
that are applied to affect tax calculations, but also the extent, proliferation, and detail of many of the individual features.

One of the most obvious examples of this is the extensive number of specific classes and tiers of property that are defined. Classification is used to determine the taxable value of a property by multiplying a classification percentage to the initial value. This changes relative burdens between different classes of property.

In 1913, Minnesota established just four classes of property. In recent years, numerous smaller classifications have been added that generally encompass a limited number of properties, often including detailed qualification criteria. Today, depending on how you count, there may be up to 55 different property classes and tiers (see "The Evolution of Minnesota's Classification System" in Appendix B).

Another example of the degree of intricate detail found in the system can be seen in how an agricultural homestead is determined. The growth of different ownership arrangements, and the substantial differences between homestead and non-homestead agricultural land, have led to incredibly meticulous requirements for qualification. The flowchart in Appendix B illustrates just how complicated this process is, and begs for a greater sense of purpose in the design of the system.

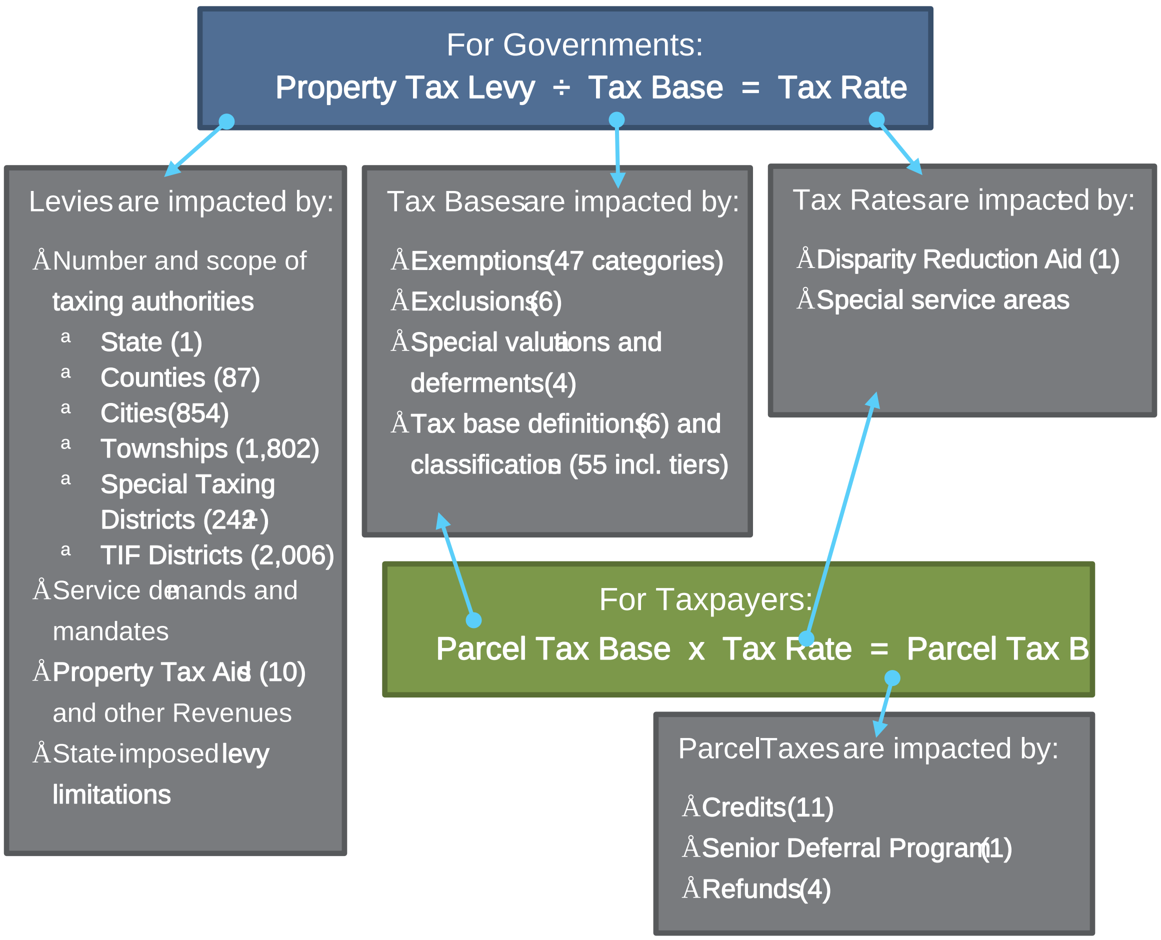


Figure 1 – Adapted from *Minnesota Department of Revenue, "Pro Tax Inventory,"* November 2010, p. 3. Counts provided in parentheses after each feature are from 2010.

A full inventory and description of the complexity of Minne[sota's system] took a substantial share of the Working Group's time. While we cannot adequately itemize all of those elements here, Appendix D and the list of Resources at the end of this report contain valuable details about many of these features.

The Consequences of Complexity and the Case for Simplification

The first reaction to demonstration of all the complexity in a tax system might often be to question:

- So what's the problem?
- Why does it matter that Minnesota's proper
- If simplicity and fairness can be competing

These are valid questions, and certainly there is an important justification for many individual features that contribute to the complexity of the system as a whole. But, complexity does generate real problems that undermine important tax principles.

Diminished Understanding for Taxpayers

When complexity is too great, taxpayers have little hope of identifying how their taxes are specifically calculated. This breeds anger and distrust as they are expected to take it on faith that they are being treated fairly and correctly. They do not know how to keep state and local government officials accountable for outcomes and hear mixed messages that they cannot assess. They are unable to plan for and adapt to changes.

Diminished Understanding for Policy Makers

When state policy makers cannot easily learn and understand the system, they are unable to adequately assess the merits of proposals and to accurately assess the outcomes of their actions. They are unable to explain issues to taxpayers with confidence. Incremental changes for narrow interests are viewed without full understanding of their costs and consequences. The ability to grapple with broad reforms is handicapped. Policy making becomes reactionary rather than strategic. Local officials may make levy decisions with good intentions but not realize their outcomes.

Diminished Understanding for Administrators

When those who administer the system cannot easily understand the interactions and outcomes, they must place blind faith in systems. Uniformity in administration is placed at risk. The ability to proof and check outcomes is diminished. The opportunity for errors in administration increases substantially. They are unable to provide full explanations to taxpayers and proper guidance to elected officials.

Diminished Transparency and Accountability

Without understanding there cannot be transparency. Without transparency there cannot be accountability. Without accountability, a system can become ineffective, inefficient, and inequitable. Problems cannot be easily identified and addressed. Costs cannot be readily verified and objective evaluation can be usurped by political messages.

Leads to Unintended Consequences and Inequities

The extensive interactions in a complex and non-transparent system can cause outcomes and other consequences that are not foreseen, not desirable, and not equitable. The presumed benefit cannot be fairly measured against unseen costs, and measures may be implemented that would otherwise fail the implicit cost/benefit analysis of policy makers.

Leads to Errors

Errors are difficult to avoid when understanding, transparency, and efficiency are compromised by complexity. The ability of administrators to identify, anticipate, and avoid errors of all magnitudes is increasingly compromised as the level of interactions and subsidies rise. Errors, of course, are generally costly, inefficient, unjust, and/or unfair.

Allows Incrementalism to Trump Global Principles

Incremental changes—where a change is made on the margin to impact a limited segment of a bigger system—are not inherently or always problematic. However, incremental changes should be made with an eye towards the broader context of more global principles so that they can be evaluated properly in terms of their consequences, trade-offs, and less tangible, cumulative costs. When the system cannot be easily understood or evaluated, the more immediately evident and more tangible value-"benefi[illegible]um and the system can stray from broader goals and principles.

Inefficiencies and Costs Rise

The more complex the system, the more difficult and inefficient it becomes to administer. Costs rise significantly. This is especially a problem with property taxes since most of the administrative costs are born locally and are not fairly evaluated by policy makers because it does not affect their budget constraints. The spillover costs of complexity, however, do rise for both state and local administrators and the feasibility of accurate administration diminishes in real terms.

A Call to Action

Although it might be easy to incrementally add a feature of complexity to the property tax system and realize a marginally improved fairness while only contrib- uting to the “costs” of complexity, cumulative costs have a much [...] a way of degrading the benefits and magnifying the costs. An inefficient system that cannot be understood, that lacks transparency and accountability to a significant degree, and that results in unintended consequences and error at a growing rate, is not an acceptable system. Periodic reform and simplification is an overdue necessity. Whether the Legislature can tackle a major redesign, or simply engage in some meaningful pruning, changes are necessary to improve the health of the overall system.

Guiding Principles

We recommend the legislature adopt the following guiding principles when proposing changes to the property tax system.

Defend the purpose

The purpose of the property tax is to provide a local revenue source to pay for local services. Although the state should define a uniform structure, the tax should be accountable to local people and the very limited ... It should not be a ... local governments s... for state legislators to serve constituent interests. The property tax is a local revenue system, not a vehicle for state policies.

Base property taxes on market value (true ad valorem system)

Using a value other than the full estimated market value (by applying exclusions, limitations, or alternate values) creates confusion, complexity, costs, and distortions.

Base property taxes on property attributes, not ownership or occupancy

The characteristics and use of a property should drive property tax levels, while the characteristics of an owner or occupant should be delivered via income tax benefits or other means. Primary benefits for individuals should be via the property tax refund programs. A “house is a house” and should be taxed the s... This principle is not intended to single out or devalue any particular group or benefit. But there may be other ways, outside of the property tax system, to achieve these same goals.

Defend broad-based goals from narrow interests

Creating new classifications or other benefits for individual or narrow subgroups of property can often be rationalized on the margin — almost everyone has a reason they should pay less. Narrowing the discussion perpetuates complexity and the incremental erosion of broad policy goals. Administrative costs can even outweigh very narrow benefits. “Commercial/industrial” is a better ... than res... for-profit recreational property, or marinas.

Consider more transparent alternatives

When evaluating new property tax proposals, legislators should consider: 1) whether a special provision is needed in the property tax system, 2) if there are other ways to deliver the benefit outside the property tax system, and 3) whether it is appropriate as a long-term benefit or a short-term fix. The property tax should not be used simply to avoid direct state costs.

Provide sunsets to prompt review

Any new changes, programs, or benefits in the property tax system should have a sunset so as to force re-evaluation over time. Sunsets will help remove provisions which are obsolete or no longer achieving their intended goals. These reviews will help promote greater efficiency and effectiveness in addressing policy goals.

Require value or intention statements on new legislation

County administration is an arm of state government and there should be a greater recognition of partnership and sensitivity to administrative costs. Therefore, when enacting new provisions, the legislature should include a statement that describes:

- why the change is necessary,
- why the change is valuable (fiscal analysis),
- what the change intends to do, and
- what alternatives were considered.

Such statements will enable the provision to be evaluated over time, and will enrich decision-making when the provision is set to expire

Make simplicity and transparency a priority

This Working Group was created to simplify the system and recommend ways to make it more understandable. A transparent and understandable system facilitates trust and accountability. A simple system is more efficient and less susceptible to unintended outcomes, and high costs. Policymakers need to defend these important principles.

Require local impact notes for any property tax changes

Although local impact notes (i.e. fiscal notes for local governments) may be requested by legislators at any time, such requests rarely take place. We recommend that local impact notes be required for all proposed changes to the property tax system to increase accountability.

Our Recommendations

Classification

We recommend the legislature implement the following changes related to the classification system in order to make it simpler, efficient, understandable, and equitable for taxpayers and administrators.

1 Reduce the number of classifications

The Minnesota Constitution's Uniformity [illegible] allows for different types of property to be classed at different rates. Minnesota's property tax is [illegible]fied in comparison to other states. Although Minnesota has up to 55 different classifications and tiers, there are truly only nine different class rates assigned to the variety of distinctions. Greater consolidation around a more limited set of class rates should be pursued.

Principle-based Recommendations

Benefits targeting specific properties or owners should not be given through classification. This can be a hidden way to shift burdens among the tax base. A benefit on one property incrementally increases taxes on all other properties. It also encourages the further creation of new, specific classifications that narrowly pick winners and losers. Other states generally have just a few classifications. (While it can be difficult to identify and count classifications, South Dakota might be second with 14, while Wisconsin has seven, Iowa has five, and North Dakota has four.)

Strong consideration or discussion should be had as to whether the system cannot simply be based on a single classification. For what purpose is any classification needed?

At a minimum, any new classifications should have an impact on a significant number of properties/owners, not a select few.

Specific Recommendations

We recommend reducing the number of classifications and tiers from 55 to 4 broad classes (see the class rate table in Appendix C for reference):

- Residential — 1a, 1d, 2a (HGA), 4a, 4b(1), 4b(2), 4b(3), 4b(4), 4bb(1), 4bb(2), 4c(4), 4c(5)(i), 4c(5)(ii), 4c(9) first 3 units, 4c(12), and 4d

  This includes classifications for residential homesteads; migrant housing; the house, garage, and first acre (HGA) of agricultural homesteads; apartments; various non-homestead residential classes; post-secondary student housing; manufactured home parks and coops; the first three units of bed and breakfasts; seasonal residential (cabins); and qualified low-income housing.

- Commercial — 1c, 3a, 3b, 4c(1), 4c(2), 4c(3)(i), 4c(3)(ii), 4c(6), 4c(9) beyond first 3 units, 4c(10), and 4c(11)

  This includes “Ma & Pa” resorts; co… and railroad property; commercial seasonal (resorts); qualifying golf courses; non-profit community service-oriented organizations; metro non-profit recreational property; the remainder of bed and breakfast units; seasonal restaurants on a lake; and marinas.

- Agricultural — 2a, 2b, and 2c

  This includes agricultural land, rural vacant land, and managed forest land.

- Other — 2d, 2e (if not elminated), 4c(7), 4c(8), 5(1), and 5(2)

  This includes private airport land; land with aggregate deposits, certain non-commercial aircraft hangars, unmined iron ore, and all other property not otherwise classified.

These classifications reflect several notions that the Working Group has embraced:

- The current residential classes make too fine of distinctions. While “apartments,” “cabins,” and “homestead” concepts may form arguable distinctions, there is also strong logic in the broader notion that a “house is a house.” Full consolidation of residential classes would yield the greatest simplification. “Homestead” benefits do n… fication distinction.

- The various classes of “business” or “commercial” property are also too finely specified. Even when a subgroup like a “resort” is identified, th… goes even further by perpetuating finer categories such as bed & breakfast, or by making distinctions based on the residency of a resort owner. The greatest simplification argues against this proliferation of narrower classifications.

- Likewise, the notion that “agricultural land is agricultural land” provides simplification and is logically more appealing than tying agricultural classifications to ownership arrangements. A single agricultural classification would not affect the valuation of different types of land, such as forest vs. rural vacant land or tillable vs. non-tillable.

2 Homestead benefits ð Expand the Property Tax Refund program

Ideally, homestead benefits would not be necessary given that they are more attributes of owners than attributes of property use. However, there are strongly held beliefs that homestead preferences serve an important role in promoting home-ownership and strong communities, among other purposes.

The Working Group acknowledges the importance of homestead benefits, and recommends that such benefits be provided via the Property Tax Refund (PTR) program in order to minimize complexity. Homestead benefits currently provided in other ways, including the homestead exclusion and disabled veterans exclusion, should be moved into an expanded homeowner PTR program.

We also recommend standardizing the definit
and one acre (HGA) for all homestead properties. These recommendations apply to both agricultural and residential homesteads.

3 Avoid or eliminate tiers and parcel-linkage

Tiers within all classifications that are based on values should be eliminated/phased out, minimized, or be replaced by alternate forms of relief. Tiers, and other requirements that cause multiple parcels to be linked together into groups by ownership, no longer view property on its own characteristics and instead evaluate ownership.

Parcel-linkages create significant complexity and confusion for taxpayers. For example, the agricultural tier confuses owners when one of their parcels sees a large increase in tax compared to other parcels and this is simply due to how the tiers are applied. The linkages make data programming and management auditing substantially more difficult and costly.

Eliminating tiers removes the need to chain parcels which makes the system less complex and reduces administrative costs.

4 Revamp the agricultural homestead classification process

The process of determining agricultural and special agricultural homesteads is very burdensome and confusing for property tax administrators and taxpayers. (See chart in Appendix B.) The various ownership arrangements and the ability to chain parcels for homestead benefits has created a complicated proliferation of qualifying criteria, and simplification of this process would make for significantly more efficient and understandable administration.

Specific Recommendations

As a result of consolidating classifications and eliminating as in *Recommendations 1 and 3*, all agricultural land and buildings (except the residential house, garage and one acre "HGA" portion) would be taxed at a single rate, regardless of ownership and with no limitations on acreage or valuation. These simplifications mean that partial interests, special agricultural homesteads, fractional, relative, cross country, and actively farming classifications would no longer be necessary. This would create a considerably more simple, efficient, transparent, and understandable system.

Within this vision, homestead requirements and benefits for agricultural properties would be the same as for non-agricultural residential properties. Homestead benefits would be limited to the HGA and would not extend beyond the first acre. Agricultural land owned by partnerships, LPs, LLCs, LLLPs, etc. would no longer qualify for "homestead," bu

receive the same treatment as all other agricultural land. The HGA would be subject to all voter approved and capital improvement referendums, while agricultural land would not.

5 Establish an agreed upon relationship ("ratio") between classification rates

Policymakers have too often viewed class

els" for benefits which can be given. However, should aim to, classi

establish relative property tax burdens between classifications, by identifying a percentage of value that should be taxed. This begs for broader classifications and a philosophical evaluation of relative burdens, not constant tinkering and discounting. Maintaining consistent ratios would enhance transparency. If rates change, they should be proportional or agreed upon changes in relationships.

Timing and Calendar Changes

Changes to the property tax calendar and elements of timing.

6 Consoldate reporting, application, and effective dates

There are a wide range of dates to track within the system as to when various appli-

cations and reports are due and when cha

tive. Consolidating around a few key dates will make it easier to understand, explain, and comply. (See proposed calendar on the following page.)

Proposed Date	Items Due (Old due date in parentheses)
Jan 2	Á Assessment date (Jan 2) Á Personal property classified as taxable or exempt (Jan 2)
Feb 1	Á Local assessors to deliver assessment records to county assessor (Feb 1)
Mar 1	Á Assessor to notify township and city clerks of local board dates (Feb 15)
Mar-Apr	Á Valuation notices mailed (Mar-Apr)
Apr 1	Á Last day to mail property tax statements (except manufactured homes) (Mar 31) Á Spring Mini abstract due (Apr 1)
Apr 1-Jun 1	Á Local Boards of Appeal and Equalization convenes (Apr 1-May 31)
May 1	Á Class 1c or 4c(5) resort applications (Jan 15) Á File for exemption (Feb 1) Á File tax court petition for dispute over value for current year taxes payable (Apr 30) Á Class 4c(3)ii, Green Acres, Class 2c applications (May 1) Á Assessor to return manufactured home assessment books to auditor (May 1) Á Homestead applications for manufactured homes (May 29) Á Metropolitan Agricultural Preserves applications (Jun 1) Á Assessors notify property owners of contamination value (Jun 1) Á Senior citizen property tax deferral, Disabled Veterans applications (Jul 1) Á Notify assessor of entity-owned property for agricultural homestead status (Jul 1) Á Class 1b applications (Oct 1)
May 15	Á First-half real property taxes due (for most properties) (May 15)
May 1-July 1	Á State Board of Equalization convenes (Apr 15-Jun 30)
Jun 1	Á Assessor notify Revenue of changes made to Spring Mini abstract (Jun before) Á Assessor sends summaries of assessment to auditor (Jun 3rd Mon)
Jul 1	Á Commissioner of Revenue to certify changes in assessments from State Boards (Jun 3 Á Cut-off date for changes in taxable/exempt status for current assessment year (Jul 1) Á All real and personal property assessments finalized (Jul 1) Á Last day to mail property tax statements for manufactured homes (Jul 15)
Aug 1	Á First-half property tax on manufactured homes due (Aug 1) Á Assessors certify commercial-industrial NTC to auditors for fiscal disparities (Aug 5)
Sep 1	Á Property Tax Refund Form M1PR (Sep 1) Á Assessors file Abstract of Assessment, Fall Mini, Market Value by Parcel File (Sep 1)
Oct 1	Á Assessors certify approval of Open Space applications for current year (Oct 15)
Oct 15	Á Second-half real and personal property taxes due (including class 2a) (Oct 15, Nov 15)
Nov 1	Á Open Space applications for next assessment year (Nov 3)
Dec 1	Á Establish homestead, publish notice of homestead application due dates (Dec 1) Á County assessor may examine appraisal records of local assessors (Dec 1)
Dec 31	Á Homestead applications for current year Á Assessor file corrections of clerical/admin errors made after local/county boards (Dec 3 Á Expiration of terms of county assessors (every 4th year) (Dec 31) Á Add or remove tax-forfeited property (Dec 31)

7 Base assessments on the most current economic conditions

When the sales that are examined to make and evaluate assessments are based on a lagged period, or are adjusted to a time that is behind the assessment date, the tax burdens can seem disconnected from current economic conditions and foster distrust in the system. Recent changes in the sales analysis process have been made to limit the lag. Assessments are now being measured against an estimate of the current-year market rather than an estimate of the previous-year market. Further and continued evaluation should aim to optimize the connection to the current market.

We recommend adjusting market definitions (a larger geographic area rather than a longer timeline) for sales comparison purposes. We also recommend the legislature encourage the transition to Electronic Certificates of Real Estate Value (eCRV) to improve responsiveness to economic conditions.

Truth in Taxation (TNT) and Notices

The process of communicating how budgets impact taxes needs significant change: notices may be too late, budgets are established much earlier, and the most important information is not well communicated.

8 Make improvements to the Truth in Taxation (TNT) process

In addition to the recommendations for all property tax-related notices and statements listed in *Recommendation 9*, the entire TNT process should be modernized and made more transparent, understandable, timely, and efficient for taxpayers and administrators.

- Basic budget information or links should be shown on the TNT notices rather than just the property specific tax amounts. The notices should also direct taxpayers to official local government websites, where more in-depth budget information would be available.
- Any "published" information should be chan… ernment websites rather than newspaper publication.
- Taxpayers should be engaged electronically (email, electronic newsletters, online forums, Twitter, etc.), rather than via in-person hearings.
- The time for constructive engagement should coincide with actual budgetary deliberations and not occur so late in the year.

9 Make improvements to notices and statements

The TNT notice, valuation notice, and tax statement need a greater sense of coordination and consistency. These tax documents should have a specific branding to improve recognition and understanding. In addition:

- Both estimated market values and taxable market values should be provided on notices.
- Websites and email contact information should be included in addition to, or in place of, addresses and phone numbers.
- Better timing/coordination of notices to maximize effectiveness should be explored.
- Notices should be available by electronic delivery.

Operational and Administrative Changes

Changes to the overall property tax system and how it is administered.

10 Investigate and plan for an eventual statewide computer system

Counties currently replicate programming and administrative overhead across a handful of consortia-based or individual systems. This duplication increases administrative costs and enables non-uniform administration. The state should explore a centralized system (whether developed or delivered via a single contracted vendor). A centralized tax system may be separate from centralized computer assisted mass appraisal system.

A state system would likely save total state and local costs, but it would transfer those costs to the state. One advantage of this would be improved accountability and a stronger disincentive to marginal changes to the property tax system, because such changes would require fiscal notes and state accountability for administrative costs. (Currently, substantial costs are borne locally and viewed without any fiscal note considerations by the state. Local impact note requests are rare.) Moving to a statewide system would help support local administration of the tax.

Such a system would take planning and a significant investment. The timing should be mindful of recent investments made by counties in their systems.

11 Convert the tax capacity system to an assessed value system

The current tax capacity system is unique to Minnesota. Along with its unfamiliar terminology, this system expresses the taxable value of property in very small amounts that are less than 2% of a property's marke The original notion was that these values would approximate tax levels and that total tax rates would typically range around 100%. Such high nominal tax rates may make comparisons with other states more difficult and possibly hurt competitiveness, even if the resulting tax burdens are competitive. Other states use a system of assessed values where the taxable value of a property is expressed as a (higher) share of the total market value. By expressing taxable value in terms that fit the scale of a market value, the tax rates are much smaller in nominal terms. Tax rates are frequently expressed as mill rates (dollars raised per $1,000 of value).

Minnesota's unique system is less transparent to out of state businesses or new arrivals. We therefore recommend converting to a more traditional assessed value system. Although this change may cause confusion in the short term, the Working Group believes that the long term advantages outweigh the initial inconveniences. Using assessed values and mill rates could yield the same calculated tax amounts, and would just change the mathematical expressions to more traditional terms. The intended result is for a more understandable and competitive property tax system.

12 Eliminate the use of property taxes for state funding

Taxpayers see the property tax as a local tax. The state property tax – paid only by commercial/industrial and seasonal recreational property – adds another layer of complexity to the system.

Within this vision, we recommend eliminating the state tax for the purpose of restoring property taxes as a local tax. Deliberations as to burden levels across property types and revenue compensation are outside the scope of the Working Group. The Working Group recognizes the budgetary implications of this recommendation. If the state property tax continues to be levied, the revenue should stay within the local system and be given directly to school districts and other local units of government, not deposited in the state general fund.

13 Avoid limits, caps, and freezes

Limits, caps, or freezes on values shift taxes, often to perverse degrees over time, resulting in unintended inequities that can be avoided by more overt classification/programs. Value limitations should be avoided.

Limits, caps, or freezes on tax amounts create gaps between levies and collections that undermine budgeting while also creating equity concerns. Tax limitations or freezes should be avoided.

Limits, caps, or freezes on levies might best constrain overall tax amounts but they can also be stimulative, overly restrictive, or ineffectively loose depending on their design, making them inefficient and undesirable. As a local tax, the state should let local governments make their own determinations and be accountable to local voters. Levy limits should not be imposed by the state.

Other Property Tax Preferences and Benefits

Specific recommendations for current programs and features of the property tax s

14 Exclusions

Exclusions reduce the taxable market value of a property and, therefore, shift the tax base. They may be seen as an easy way to provide a benefit because they do not cost the state money. Exclusions are less transparent and less understandable for taxpayers, who may not know that they're benefit or why the value of their neighbor's house is

Principle-based Recommendations

The state should pay for benefits that the state thinks important (e.g. use credits or re-r funds, rather than exclusions or exemptions). If used, exclusions should be tied to the property, not the owner. Because exclusions are not very responsive, they should not be used to provide short-term or one-time benefits.

Specific Recommendations

Exclusion	Recommendation (or Options)	Reasons
This Old House	• Allow to phase out	• Did not necessarily achieve intended goals • Not transparent
This Old Business	• Allow to phase out	• Did not necessarily achieve intended goals • Not transparent
Plat Law	• Delete, or • Phase out	• Let market forces determine value (true ad valorem) • Developers can choose when to plat
Mold Damage	• State paid property or income tax credit • State Refund • Abatement reimbursed by the state	• State should pay for benefits that it finds important • Exclusion is not responsive to when you pay to clean u these other options are.
Disabled Veterans	• State Refund • Income tax credit	• Based on owner, not on property • Some areas with a large percentage of disabled vetera in their communities have seen a large reduction in thei tax base.
Homestead Exclusion	• Eliminate as a consequence of other recommendations.	• Based on owner, not on property • See Recommendation 2.

15 Credits

Credits reduce the final tax you owe. They do not shift the tax base, but they do cost the state money. Credits may be more accountable and understandable for taxpayers (tax credits = what you pay).

Specific Recommendations

Credit	Recommendation (or Options)	Reasons
Disaster (2 credits, 1 abatement)	ÁKeep as is	ÁThese credits/abatements are successful and responsiv ÁAlready have built-in time limit (not everlasting) ÁLocal options allows some local control
Power Line	ÁDelete, or ÁPhase out	ÁHigh administrative cost (calculating a separate tax bas and rate) for relatively small benefit ÁPossible overlapping of benefits: Properties may alreac have a lower valuation due to the power line and/or money from an easement for the line.
Disparity Reduction	ÁKeep as is	ÁKeeps businesses in the state. Paid for by state as a st objective. As a credit, it is accountable in the system
Agricultural Homestead Market Value Credit	ÁEliminate as a consequence of other recommendations	ÁIf HGA receives homestead benefits as a residential homestead and all ò a glr i lca at the same rate, this credit would no longer apply.
Bovine Tuberculosis Credit	ÁDo not reinstate	ÁExample of a non-property tax related benefit in the property tax system ÁAddressed a one-time issue and allowed to expire according to original intent

16 Exemptions

Exemptions shift the tax base but do not cost the state money. Property that is exempt is removed from the tax rolls entirely in order to accomplish public purposes (rather than to favor certain property owners over others).

Principle-based Recommendations

The legislature should be very selective as to which properties should pay no property tax at all. Permanent exemptions should not exist to serve special interests. When properties are removed from the tax rolls they can seem hidden or be forgotten, reducing accountability in the system. Therefore, real property exemptions should have automatic review/sunset dates to improve accountability and ensure they are still necessary in achieving their intended goals.

Specific Recommendations

Exemptions	Recommendation (or Options)	Reasons
Constitutional/Federal	Á Keep as is	Á Not changing constitutional exemptions
JOBZ	Á Allow to phase out	Á Phasing out was original intent.
Business Incubator Property	Á Allow to phase out	Á Phasing out was original intent.

17 Aids

State aids supplement property taxes for local governments. *Local Government Aid (LGA), County Program Aid (CPA), and pension aids are property tax related, but the Working Group has not made recommendations on them because they are being worked on by other study groups.*

Specific Recommendations

Aids	Recommendation (or Options)	Reasons
Utility Valuation Transition Aid	Á Allow to phaseout	Á Original intention is to naturally phaseout after transition from utility rule change.
Disparity Reduction Aid (DRA)	Á Sunset Á Phaseout	Á Created for 1988 conversion from mill rates to NTC; may not be achieving intended purpose in all areas

18 Special Valuations and Deferrals

Special valuations and deferral programs have the effect of reducing the amount of taxable value for qualifying properties. While these programs may create benefits for participants, they also increase complexity, decrease accountability and transparency, and make the system less efficient.

For example, Open Space and Green Acres establish value for tax purposes that is less than the prop, which is a õ difficult exercise. There is also more room for problems and errors when you move away from fair market values.

All current and any future special valuation or deferral programs should have sunset dates to prompt reevaluation.

19 Refunds

After property taxes are paid, qualifying property owners may apply for a refund for a portion of their property taxes. Refunds are paid for by the state. Homeowner and renter Property Tax Refunds (PTR) are income-tested, while special targeting PTR and some other programs are not.

Principle-based Recommendations

The refund should be a key tool for addressing equity issues that relate to owners of property. The state should pay for relief that it chooses to grant, as opposed to exclusions, classifications, or other features that cause tax shifts.

Specific Recommendations

Refunds / Other	Recommendation (or Options)	Reasons
Homeowner PTR	• Expand use	• Should be the primary method of providing benefits tied to ownership or occupancy, including homestead and other benefits • Paid for by state as state objective. • See Recommendation 2.
Renter PTR	• Reevaluate it	• Classifying all residential property equally lowers the ra paid by apartments and thus the refund serves less need.
Homeowner "Targetin	• Keep it	• This may be a valuable tool to address the impacts of implementing the recommended changes.

Appendices

Appendix A: About the Property Tax Working Group

Legislative Charge

Minnesota Statutes, section 270C.991, subdivision 4

Property tax working group (a) A property tax working group is established as provided in this subdivision. The goals of the working group are:

(1) to investigate ways to simplify the property tax system and make advisory recommendations on ways to make the system more understandable;
(2) to reexamine the property tax calendar to determine what changes could be made to shorten the two-year cycle from assessment through property tax collection; and
(3) to determine the cost versus the benefits of the various property tax components, including property classifications, credits, aids, exclusions, exemptions, and abatements, and to suggest ways to achieve some of the goals in simpler and more cost-efficient ways.

(b) The 12-member working group shall consist of the following members:

(1) two state representatives, both appointed by the chair of the house of representatives Taxes Committee, one from the majority party and one from the largest minority party;
(2) two senators appointed by the Subcommittee on Committees of the Senate Rules and Administration Committee, one from the majority party and one from the largest minority party;
(3) one person appointed by the Association of Minnesota Counties;
(4) one person appointed by the League of Minnesota Cities;
(5) one person appointed by the Minnesota Association of Townships;
(6) one person appointed by the Minnesota Chamber of Commerce;
(7) one person appointed by the Minnesota Association of Assessing Officers;
(8) two homeowners, one who is under 65 years of age, and one who is 65 years of age or older, both appointed by the commissioner of revenue; and
(9) one person jointly appointed by the Minnesota Farm Bureau and the Minnesota Farmers Union.

The commissioner of revenue shall chair the initial meeting, and the working group shall elect a chair at that initial meeting. The working group will meet at the call of the chair. Members of the working group shall serve without compensation. The commissioner of revenue must provide administrative support to the working group. Chapter 13D does not apply to meetings of the working group. Meetings of the working group must be open to the public and the working group must provide notice of a meeting to notify interested pe sons at least seven days before the meeting. A meeting of the working group occurs when a quorum is present.

(c) The working group shall make its advisory recommendations to the chairs of the House of Representatives and senate Taxes Committees on or before February 1, 2013, at which time the working group shall be finished and this subdivision expires. The advisory recommendations should be reviewed by the Taxes Committees under subdivision 5.

Members

Kathleen A. Gaylord (Chair)
Dakota County Commissioner
Association of Minnesota Counties

Rep. Denise Dittrich
Minnesota House of Representatives

Rep. Greg Davids
Minnesota House of Representatives

Sen. Rod Skoe
Minnesota Senate

Sen. Warren Limmer
Minnesota Senate

R. Thomas Mould
Homeowner (under age 65)
Minnesota Department of Revenue

Eric Sorensen
Homeowner (age 65 or older)
Minnesota Department of Revenue

Luayn Murphy
City Administrator, City of Mayer
League of Minnesota Cities

Rob Vanasek
Vanasek Consulting
Minnesota Association of Townships

Matt Van Slooten
President, Carlson Real Estate Company
Minnesota Chamber of Commerce

Stephen Behrenbrinker
Assessor, City of St. Cloud
Minnesota Association of Assessing Officers

Chris Radatz
Public Policy Director,
Minnesota Farm Bureau
Minnesota Farm Bureau and Minnesota Farmers Union (Joint Appointment)

Alternates* & Former MembersÀ

- Rep. Linda Runbeck*
  Minnesota House of Representatives
- Sen. Rick OlseenÀ
  Minnesota Senate
- Jason NordÀ
  Minnesota Department of Revenue
- Cal LarsonÀ
  Homeowner (age 65 or older), Minnesota Department of Revenue
- David FrickeÀ and Gary Pedersen*
  Minnesota Association of Townships
- Craig Patterson* and Doug Fulton*
  Minnesota Chamber of Commerce
- Bill Effertz*
  Minnesota Association of Assessing Officers
- Thom Petersen*
  Government Relations Director,
  Minnesota Farmer's Union
  Minnesota Farm Bureau and Minnesota Farmers Union (Joint Appointment)

Appendix B: Examples of Complexity

The Evolution of Minnesotaõs Classifi

1913		
Class	**Description**	**Ratio**
1	Iron Ore Mined or Unmined	50%
2	Household Goods and Personal Effects	25%
3	Unplatted Real Estate	33⅓%
3	Livestock, Farm Produce, Inventories	33⅓%
3	Manufacturers' Tools	33⅓%
4	All Other Property (primarily Urban Real Estate)	40%

1933		
Class	**Description**	**Ratio**
1	Iron Ore Mined or Unmined	50%
2	Household Goods and Personal Effects	25%
3	Unplatted Real Estate	33⅓%
3	Livestock, Farm Produce, Inventories	33⅓%
3	Manufacturers' Tools	33⅓%
3a	Agricultural Machinery and Horses Used by the Owner and Agricultural Products in the Hands of the Producer	10%
3b	Unplatted Real Estate Used For a Homestead	
	First $4,000	20%
	Excess	33⅓%
3c	Platted Real Estate Used For a Homestead	
	First $4,000	25%
	Excess	40%
4	All Other Property	40%

1953		
Class	**Description**	**Ratio**
1	Iron Ore Mined or Unmined	50%
1a	Low Recovery Iron Ore	30-48½%
1a	Blast Furnace Products	15%
2	Household Goods and Personal Effects	25%
3	Rural Real Estate	33⅓%
3	Agricultural Products, Inventories	33⅓%
3	Manufacturers' Tools	33⅓%
3	Structures on Fed/State Lands	33⅓%
3a	Agricultural Products in the Hands of the Producer	10%
3b	Rural Real Estate Used For a Homestead	
	First $4,000	20%*
	Excess	33⅓%
3c	Other Real Estate Used For a Homestead	
	First $4,000	25%*
	Excess	40%
3cc	Disabled Veterans' Special Housing	
	First $8,000	5%
	Excess	40%
3d	Livestock, Poultry, Horses, and Mules; Agricultural Tools, Implements, and Machinery	20%
-	Petroleum Refinery Real Property	27%
-	Pretroleum Refinery Personal Property	17%
4	All Other Property	40%

1973		
Class	**Description**	**Ratio**
1	Iron Ore Mined or Unmined	50%
1a	Low Recovery Iron Ore	30-48½%
1a	Blast Furnace Products	15%
2	Household Goods and Personal Effects**	25%**
2a	Mobile Homes	
	Homestead First $12,000	25%
	Homestead Excess	40%
	Non-Homestead	40%
3	Agricultural Land	33⅓%
3	Tools, Implements and Machinery which are Fixtures	33⅓%
3	Personal Property on Fed/State Lands	33⅓%
3	Commercial and Non-Commercial Seasonal Residential for Recreational Purposes	33⅓%
3b	Agricultural Homestead	
	First $12,000	20%*
	Excess	33⅓%
3c	Other Real Estate Used For a Homestead	
	First $12,000	25%*
	Excess	40%
3cc	Parapalegic Vets/Blind Homestead	
	First $24,000	5%
	Excess - Agricultural	33⅓%
	Excess - All Other	40%
3d	Non-Homestead Residential	40%
3e	Timber Land	20%
3f	Owner Occupied Residences on Leased Land	(3b, 3c, 3cc)
3h	Petroleum Refinery Real Property	30%
-	Parking Ramp in Certain First Class Cities	25%
-	Housing for the Elderly or for Low and Moderate Income Families Financed by Federal Loan or Federally Insured Loan Pursuant to Title II	
	Municipalities of 10,000 or more	20%
	Municipalities under 10,000	5%
4	All Other Property	43%

*Exempt from state tax except old debt.
**1959 Law allows county boards to exempt class 2 property.