SUBJECT: Changing scope, process for binding arbitration on appraisal value protests

COMMITTEE: Local Government Ways and Means — committee substitute recommended

VOTE: 7 ayes — Hill, Creighton, Elkins, C. Howard, Puente, Quintanilla, Villarreal

0 nays

WITNESSES: For — James Popp, Texas Association of Realtors; Joseph M. Harrison, IV; Jim Robinson; (*Registered, but did not testify:* Daniel Gonzalez, Texas Association of Realtors; David Braun; Cassie Gresham)

Against — David Kaplan

On — Michael Amezquita, Bexar Appraisal District; Michele Gregg, Texas Apartment Association; (*Registered, but did not testify:* Connie Heyer, Texas Self Storage Association; Gerald "Buddy" Winn)

BACKGROUND: Texas Constitution, Art. 8, sec. 18 requires a single appraisal of the market value of all property in a county subject to ad valorem taxation.

Under Tax Code, ch. 41, property owners may protest appraisal districts' valuation of their property when suspected errors might adversely affect the owner's concern, including:

- market value;
- unequal appraisal;
- inclusion or exclusion of property on the property tax roll;
- qualification for agricultural or timber status;
- appraisal district authority to make value determinations;
- ownership; or
- change of land use.

Tax Code, sec. 41.01 establishes an appraisal review board (ARB) to hear protests by property owners regarding appraised value of their property. When a property owner files a protest with the county appraisal district (CAD), the ARB issues decisions on such disputes. An ARB is required to:

- determine protests initiated by property owners;
- determine challenges initiated by taxing units;
- correct clerical errors in appraisal records and appraisal rolls; and
- determine proper granting of exemptions

Tax Code, ch. 42 allows a property owner to appeal ARB decisions to district court.

In 2005, the 79th Legislature approved HB 182 by Mowery, establishing appeal through binding arbitration for certain property owners through the creation of Tax Code, ch. 41A. For property valued at $1 million or less, the appraisal district is required to notify property owners of this option. Within 45 days of receiving notice of an ARB decision, a property owner seeking to appeal through binding arbitration has to make a deposit of $500 payable to the comptroller, 10 percent of which can be retained to cover administrative costs. A chief appraiser has 10 days to certify a request and forward it to the Comptroller's Office, which sends both sides a list of eligible arbiters from a registry it maintains. The appraisal district and property owner have 20 days to select an arbitrator before the comptroller selects one for them. Within 20 days of arbitration, the arbitrator is required to render a decision. The losing party is required to pay the arbitrator's fee. For the property owner, the charge can be no more than $450, or 90 percent of the initial deposit.

DIGEST:

CSHB 3194 would expand eligibility for binding arbitration as an option for property owners who did not want to appeal an ARB decision to a district court. The bill would impose additional requirements for those seeking to become and those seeking to maintain their eligibility as arbitrators under this section. It also would create formulas and procedures for an arbitrator to rule on unequal appraisal cases.

Eligibility. The bill would allow a property owner, as an alternative to appealing an ARB decision to district court, to protest the valuation of the owner's real property through binding arbitration as long as:

- the property was the owner's residence homestead;
- the appraised or market value, as applicable, was $1 million or less; or
- the chief appraiser of the district in which the protest was filed consented to an appeal through this process.

A property owner would be deemed ineligible for binding arbitration if:

- the owner was represented before the ARB by a property tax consultant, as defined by Occupations Code, sec. 1152.001; and
- the owner or consultant failed to provide copies of all evidence used in the ARB hearing to the chief appraiser at least 14 days prior to the hearing date.

Chief appraiser's consent. The bill would maintain the 10-day requirement for a chief appraiser to certify a binding arbitration request, but would provide an exemption for requests that required the consent of the chief appraiser. In those instances, the chief appraiser would have 30 days to make a decision. If the chief appraiser consented, the procedures would mirror those currently in statute. If the chief appraiser rejected binding arbitration, the appraisal district would be required to return the request form and deposit to the property owner via certified mail.

A property owner whose binding arbitration request was denied would not be allowed to protest this decision under Tax Code, ch. 41, nor could the owner appeal the decision in district court under Tax Code, ch. 42. The property owner still would have the ability to appeal the ARB decision, even if the window for filing a notice of appeal had expired, as long as the owner filed notice within 45 days of receiving notification from the chief appraiser that the case would not be considered through binding arbitration.

Eligible arbitrators. Currently, an arbitrator must be certified or licensed as a real estate appraiser, broker, or salesperson, but the bill would mandate that the person must have been continuously certified or licensed for the five years prior to the date the person agreed to serve as an arbitrator.

The bill would disqualify from serving as an arbitrator under this chapter:

- a person registered as a property tax consultant under Occupations Code, ch. 1152; and
- a person paid to provide property tax consulting services, as defined by Occupations Code, sec. 1152.001, in any appraisal district in which the person had provided those services.

The bill would allow arbitrators to remain on the registry for two years after being added. To remain for more than two years, an arbitrator would have to renew his or her agreement with the comptroller by:

- filing a renewal application with the comptroller at the time and manner established by the comptroller;
- continuing to meet the eligibility requirements; and
- completing at least eight hours of continuing education in arbitration at a university, college, real estate trade association, or legal association in the preceding two years.

Unequal appraisal. The bill would allow an arbitrator to rule in favor of a property owner in a protest of unequal appraisal only if the evidence showed:

- the appraisal ratio of the property exceeded by at least 10 percent the median level of appraisal of a reasonable and representative sample of other properties in the appraisal district;
- the appraisal ratio of the property exceeded by at least 10 percent the median level of appraisal of a sample of properties in the appraisal district with similar properties or characteristics as the property subject to the appeal; or
- the appraised value of the property exceeded by at least 10 percent the median appraised value of a reasonable and representative sample of comparable properties appropriately adjusted.

The equalized appraised value for a property owner under the sections focused on a property's appraisal ratio would be calculated by multiplying the ARB's appraised value by the median level of appraisal under the applicable section. The equalized appraised value for a property owner under the section focused on a property's appraised value would be equal to the median appraised value determined under that section. The equalized appraised value for a property owner eligible under more than one of these sections would be the lowest value.

An arbitrator ruling on a protest of unequal appraisal:

- would be required to determine each applicable median level of appraisal or median appraised value according to law;
- would not be required to adopt the aforementioned values proposed by a party to the appeal; and

- would not be allowed to limit or deny an award to a property owner who had met any of the prescribed determination methods if one of those methods was higher.

Arbitration decision. The bill would preclude an arbitrator from determining any issue or including any relief on an issue not specified by the statute. It would require that a decision in binding arbitration determine:

- the appraised or market value, as applicable, for an appeal of an ARB decision determining a protest of the property's appraised value; and
- the equalized appraised value for a decision in favor of a person appealing an ARB decision regarding unequal appraisal of property.

The appraised or market value or the equalized appraised value — or in situations in which both applied, the lower value of the two — would be used to determine which entity came closest to the arbitrator's value.

Request form. The bill would expand what the comptroller is required to state on the form for a property owner to request binding arbitration. On top of an existing requirement that the property owner state the basis for appealing the ARB decision and any other reasonably necessary information, the form also would require the owner to provide only:

- the correct appraised value of the property if it was not used for agricultural or timber purposes;
- the correct appraised or market value if the property was used for agricultural or timber purposes; and
- a request that the chief appraiser consent to binding arbitration if the property was neither the owner's residence homestead nor valued at $1 million or less.

Representation. The bill would expand the pool of people eligible to represent themselves in binding arbitration to include a certified accountant under Occupations Code, ch. 901. It also would add language to specify those representing themselves would do so at their own cost.

Effective date. This bill would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it

would take effect September 1, 2007, and would apply only to an appeal through binding arbitration requested on or after that date. Changes regarding qualifications and requirements of arbitrators would apply only to those who qualified to serve on or after the effective date.

SUPPORTERS SAY:

CSHB 3194 would amend the binding arbitration process established during the last regular session to expand the pool of those eligible to participate, raise qualification requirements for arbitrators, and include an option to challenge a property's appraisal as compared with other similar properties. The binding arbitration process has been a good option for taxpayers but is limited in both its scope and the number of participants. This bill would allow more taxpayers to avail themselves of a less costly and intimidating option than taking their cases to district court.

Since the 79th Legislature created binding arbitration for property owners to appeal an ARB decision, 583 people have used this option in lieu of taking their cases to district court. Binding arbitration provides property owners a neutral forum to air their grievances, which in turn restores public confidence in the integrity of the appraisal process. It also, in most cases, takes less time and costs less money for a property owner than it would to file an appeal with a district court. Although the arbitration process can be costly for appraisal districts, the costs of preparing for cases in district court — and paying attorney's fees in the event of a loss — also create financial burdens for the district.

The bill would implement one of the recommendations of the Texas Task Force of Appraisal Reform by allowing property owners to challenge an unequal appraisal. For a person whose property was valued at the market rate but not in line with comparable homes, the bill would provide binding arbitration as a tool to remediate that decision. By specifying a formula under which an arbitrator would be required to assess unequal appraisal, the bill would clarify vagaries within the Tax Code. Property tax consultants typically set values using median homes from the bottom end, resulting in a median value that creates a downward spiral in appraisal values. This bill would largely correct this phenomenon.

CSHB 3194 would add new requirements for those who qualify as arbitrators and for those seeking to maintain their eligibility. These measures would provide additional quality control to ensure an arbitrator was well versed in the property tax arena and continued to receive

guidance on the most effective ways to assess and render decisions through arbitration training.

The author plans to offer a floor amendment in response to constitutional concerns about removing interpretation and enforcement of the equality and uniformity of property taxes from the judiciary. The amendment would allow property owners to seek binding arbitration only in disputes over the value of a residence homestead or the value of property worth $1 million or less. This would offer a more conservative approach to expanding the pool of those eligible to participate in binding arbitration.

OPPONENTS SAY:

CSHB 3194 would not fix a number of the problems exposed during the first two years of binding arbitration, and any expansion of the program in either scope or participation would create more opportunities for the entire process to be challenged on constitutional grounds.

In his State of the Judiciary address this year, Chief Justice Wallace B. Jefferson raised concerns about the effect of the growing prevalence of arbitration as an option. Private dispute resolution, he said, does not allow for a full public airing of issues, nor does it lead to innovations and solutions learned from cases that could help resolve future disputes. An error committed in a private setting, he noted, has little ability to be corrected.

This bill would also impinge on the judiciary's role in a way that may run afoul of the Texas Constitution. A Texas Court of Appeals ruled that a previous statute allowing a taxpayer the unilateral right to refer a case in litigation to binding arbitration was unconstitutional in *Hays CAD v. Mayo Kirby Springs, Inc.*, 903 SW.2d 394,397 (TX 1995). The court found the process violated four different provisions of the Texas constitution by:

- delegating judicial power and process away from the courts to the arbitrator (Tex. Const., Art. 5, Sec. 1);
- violating separation of powers (Tex. Const., Art. 2, Sec. 1);
- subverting the appraisal districts' and courts' role in assuring equality and uniformity in ad valorem taxation (Tex. Const., Art. 8., sec. 1); and
- purporting to authorize secret conduct of the public task of taxation, violating requirements for an open court (Tex. Const., Art. 1, sec. 13).

Many of those same issues extend to this binding arbitration process, and some would be exacerbated by this legislation. An additional constitutional problem could arise out of the role of the comptroller's office in assigning arbitrators in certain cases because the law mandates any administrative or judicial enforcement of property tax appraisal procedures originate in the county where the tax is imposed.

Any expansion of the binding arbitration program could create additional costs to appraisal districts. Aside from the increased potential of more decisions against the district, which would reduce taxable value and force the district to pay the arbitrator's fee, the process itself is a more expensive endeavor than a court hearing because of extra travel and administrative costs.

CSHB 3194 would allow properties valued at more than $1 million, with the consent of the chief appraiser, to be considered through binding arbitration. Through such an expansion of the process, more opportunities would certainly arise for someone to challenge the constitutionality of this program. Even a nuanced approach to expanding the binding arbitration process would fail to address the central legal problem with this program.

OTHER OPPONENTS SAY:

CSHB 3194 would not go far enough to impose requirements on arbitrators and should be amended to provide for property tax training. The version reported out of committee should not be amended to remove the ability of those whose property is valued at more than $1 million to use binding arbitration as an option to appealing through district court.

Although the bill would add requirements for arbitrators to remain on the state's registry, it would not address some of the major flaws of the current system. A person with a real estate license does not necessarily have significant expertise in the area of property tax law, and this bill would not require any training on that topic. Additionally, the process varies greatly depending on the arbitrator. Any attempt to change it should include a way to standardize the procedure for conducting a hearing and the documentation and forms required for the process.

Binding arbitration should be an option for all property owners, not just those whose property is valued below $1 million. Just because someone has the money to file in district court does not mean the person should have to do that, especially when another option that could be less time-

consuming is available. Additionally, there should not be a requirement that these property owners obtain the consent of the chief appraiser.

NOTES:

The Legislative Budget Board does not anticipate that CSHB 3194 would have a significant fiscal impact on the state. If the binding arbitration workload for the comptroller grew to reflect a portion of the 1,500 annual appeals of ARB decisions currently requested via district court, the Comptroller's Office likely would seek an additional staff attorney and three additional tax professionals, which would cost $537,596 in fiscal 2008-09.

The author plans to introduce two floor amendments to CSHB 3194. The first floor amendment would:

- remove the ability of the owner of property valued at more than $1 million, other than a residence homestead, to seek binding arbitration, and remove all procedural requirements connected with that option; and
- increase the amount of money the comptroller would be allowed to retain for administrative expenses from 10 percent to 30 percent of the $500 deposit.

The second floor amendment would disqualify from eligibility for binding arbitration a person represented by anyone other than himself — not solely a tax consultant as specified in CSHB 3194 — and who failed to provide hearing evidence at least 14 days before the hearing.

HB 3194 as introduced would have opened up binding arbitration to all parties and did not include any of the other provisions in the substitute except for the sections covering arbitrator qualifications.

The companion bill, SB 1642 by Williams, has been referred to the Senate Finance Committee.