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Fall 2014

Discussing Kansas's Proposed Property Tax Averaging Payment Plan: HB 2769
An Alternative to Kansas's Property Tax Payment System for Homeowners

Executive Summary

The Kansas Constitution requires the legislature to provide a uniform and equal basis of valuation and rate of taxation for all property in Kansas. This requirement ensures that every property owner in Kansas has an equal burden of taxation in relation to all other property owners. The Kansas Legislature has set up a three-step process to ensure that all property is taxed in a uniform and equal manner: the property is valued at its fair market value; assessed at a rate as specified in the Kansas Constitution; and multiplied by the mill levy rate of the taxing district in which the property resides. As long as all property in the same class is valued in accordance with its fair market value and is taxed at a uniform and equal rate, the property will be taxed in a uniform and equal manner.

In Kansas, taxpayers can either pay the entire amount of tax on their real property on or before December 20 of each year, or pay half of the amount on December 20 and pay the second half on or before May 10 of the following year. Although taxpayers have the option to pay half of their taxes due on their real property in a given year on or before December 20, this option does not do enough to protect taxpayers whose real property taxes dramatically increase from year to year. The current property tax payment system in Kansas only allows taxpayers to defer half of their taxes due for a couple of months before they must come up with the total amount. A bill, HB 2769, introduced in the Kansas legislature in 2014 proposed an alternative payment method for qualifying property owners that aims to decrease this burden on taxpayers.

HB 2769 would allow qualified taxpayers to enter into a property tax averaging payment plan over the course of several years. The tax averaging payment plan would allow homeowners who qualify for the plan to pay a calculated amount rather than their actual taxes due on their home in a given year. The payment plan would not change the way in which property taxes are computed, but it would change how much a participating taxpayer is required to pay in a given year by averaging the taxes due in the current year with those due in the previous years in which the homeowner participated in the plan and creating a lien on the deferred taxes with accruing interest. This would give participants a reliable cushion that will lessen the burden of paying a dramatic increase in property taxes from year to year.

Although the payment plan would protect homeowners from increases in property taxes from year to year, the payment plan will dramatically affect the generation of revenue for the counties and the State. Because homeowners will be able to defer part of their payment in the years in which they participate in the plan, the taxing districts will not receive the full amount of revenue from property taxes each year. This will create uncertainty within each taxing district in determining the budget for a given year.

Residential property owners within the same taxing district may not be taxed in a uniform and equal manner as a result of the payment plan. Because homeowners are the only residential property owners who may participate in the plan, this could create an unconstitutional disparity between homeowners and other residential property owners. However the payment plan does not change how property taxes are calculated, but it would change how much a participant is required to pay in a given year. Although the payment plan will have the effect of substituting the actual taxes a homeowner must pay in a given year with a calculated amount, it will also create a lien on the portion of the actual taxes that have not yet been paid. Eventually participants will be required to pay all of the deferred taxes plus accrued interest for the years in which they participated in the plan. As long as the interest accrued is a satisfactory measure of the time value of money, participants and non-participants will be taxed in a uniform and equal manner.

Table of Contents

Introduction.....4

Current Property Tax Law4

 Constitutional Requirements.....4

 How Property is Valued in Kansas for Tax Purposes.....6

 How Property Taxes are Calculated in Kansas.....7

 When are Real Property Taxes Due and Payable in Kansas.....8

 One Concern with the Current Property Tax Payment System8

HB 2769: An Alternative to Kansas’s Property Tax Payment System.....9

 What does the Property Tax Averaging Payment Plan Do?9

 What are the benefits of the Property Tax Averaging Payment Plan?11

 Concerns with the Property Tax Averaging Payment Plan12

 Revenue and Budgetary Concerns12

 Constitutional Concerns.....13

INTRODUCTION

In Kansas, all property owners must be taxed in a uniform and equal manner. This is accomplished by a three-step process: the property is valued; assessed at a rate as specified in the Kansas Constitution; and multiplied by the mill levy rate of the taxing district in which the property resides. This process ensures that every property owner in Kansas bears an equal burden of taxation in relation to all other property owners. Property taxes are calculated and must be paid on a yearly basis. However, these taxes tend to fluctuate in some taxing districts from year to year for various reasons. Some taxpayers are concerned with the current method because it creates a heavy burden on taxpayers whose property taxes rise dramatically from year to year. Taxpayers are required to pay their property taxes every year even with a dramatic increase in amount. A bill introduced in the Kansas Legislature in 2014 proposed an alternative payment method for qualifying property owners that aims to decrease this burden on taxpayers. This paper discusses the current status of property tax law in Kansas and the proposed alternative to the property tax payment method as raised in last legislative session's HB 2769.

CURRENT PROPERTY TAX LAW IN KANSAS

CONSTITUTIONAL REQUIREMENTS

The Kansas Constitution requires the legislature to provide a uniform and equal basis of valuation and rate of taxation for all property in Kansas, unless that property is specifically exempted.¹ However, taxation in Kansas is not a purely uniform and equal system because the Constitution qualifies the requirement in three ways: it creates a system of differing assessment rates for specific classes of property; it creates exemptions for certain property from taxation; and it implicitly grants the legislature authority to create additional exemptions.² Thus, property

that is subject to taxation in Kansas must be taxed in a uniform and equal basis in relation to property within the same class.

In Kansas, there are two broad classes of property for taxation purposes: real property and tangible personal property.³ Real property includes all land and structures that are firmly attached to the land.⁴ Conversely, tangible personal property includes any movable thing that is subject to ownership.⁵ These two broad classes of property are further divided into several subclasses.⁶ Each subclass of property contains its own assessment rate, which determines the percentage of the value of the property that will be taxed.⁷ Because each class of property is broken down into several subclasses, all property that falls within a particular subclass must be taxed in a uniform and equal manner. Thus, all real property used for residential purposes in Kansas is subject to an assessed rate of 11½%.⁸

Although the Kansas Constitution requires that the Kansas legislature provide a uniform and equal basis of valuation and rate of taxation, there has been much debate as to what this requirement actually means. A uniform and equal basis of valuation essentially means that all property within the same subclass must be valued in a uniform and equal manner.⁹ A uniform and equal rate of taxation essentially means that property within the same subclass must be taxed at a uniform and equal rate.¹⁰ The policy reason for requiring a uniform and equal basis of taxation is to ensure that all taxpayers share an equal burden of taxation in relation to the value of their property that is subject to tax.¹¹ The uniform and equal requirement of the Kansas Constitution provides essentially identical protection as the Equal Protection Clause of the Fourteenth Amendment to the United States Constitution.¹² Thus, the Kansas Constitution protects property from being taxed in a different manner than property within the same

subclass.¹³ The basis of valuation or rate of taxation is irrelevant so long as the basis or rate is applied uniformly to all similarly classified property in a taxing district.¹⁴

However, if there is a systematic, arbitrary, or intentional basis of valuation or rate of taxation that causes substantially unequal treatment between taxpayers with similarly classified property, then the taxpayers are not being taxed in a uniform and equal manner.¹⁵ However, mere errors in judgment or mistakes in making assessments will not establish a constitutional violation.¹⁶ To prove that property within the same class is not being taxed in a uniform and equal manner, a taxpayer must show: that his property was not valued in a uniform and equal manner or that his property was not taxed at a uniform and equal rate; and that the lack of uniformity or inequality was the result of a systematic, arbitrary, or intentional basis of valuation or rate of taxation.¹⁷ If the valuation of a taxpayer's property is not assessed in a uniform and equal manner, then the valuation is illegal or void.¹⁸

HOW PROPERTY IS VALUED IN KANSAS FOR TAX PURPOSES

The Property Tax System in Kansas is statewide and is administered by local governments. Unless multiple counties elect to unite with each other to form a single appraisal district, each county encompasses a single appraisal unit and the county treasurer is responsible for appraising all property within the county.¹⁹ A property's appraised value determines, in part, the amount of tax a taxpayer must pay for that property in a given year.²⁰ To ensure a uniform and equal basis of valuation, Kansas law requires property to be appraised at its fair market value.²¹ Fair market value is "...the amount in terms of money that a well informed buyer is justified in paying and a well informed seller is justified in accepting for property in an open and competitive market, assuming that the parties are acting without undue compulsion."²² To

determine the fair market value of property, K.S.A. 79-503a provides a list of factors the appraiser must consider including, but not limited to, the following: the property's classification, size, location, quality, and condition; the cost of reproducing improvements; the property's sale value on an open market; and comparison with values of other property of known or recognized value.²³ Whether the taxing officials complied with K.S.A. 79-503a is essential to determine whether the appraisal was assessed in a uniform and equal manner.²⁴

After the appraiser has considered the relevant factors to determine the fair market value of the property, the appraiser then uses one or more of the following methods to value the property: the market approach, the cost approach, or the income approach.²⁵ Using the market approach, the appraiser estimates the value by looking at sales of similar property and adjusting for differences between the properties.²⁶ Using the cost approach, the appraiser estimates the value by considering what it would cost to replace or reproduce the property with depreciation taken into account.²⁷ Using the income approach, the appraiser estimates the value by considering the income the property is anticipated to produce from rent.²⁸ It does not matter whether the appraiser uses one or more of these methods to value the property as long as the property is appraised at its fair market value in a uniform and equal manner in compliance with the statutes.²⁹

HOW PROPERTY TAXES ARE CALCULATED IN KANSAS

Once a property's appraised value is determined for a given year that value is multiplied by the assessment rate, which is specified within the property subclasses of Article XI of the Kansas Constitution.³⁰ Uniformity and equality require all property classified as residential property in Kansas to be assessed at a rate of 11½%.³¹ The appraised value multiplied by the

assessment rate is the assessed value of the property.³² The assessed value is then multiplied by the tax rate, which is known as the mill levy.³³ The mill levy is set each year by the taxing districts and determines the amount of revenue that will be needed to fulfill the districts' budgetary needs.³⁴ Uniformity and equality require all property within the same class to be taxed at the same rate.³⁵ To determine the amount of tax a taxpayer must pay on a specific property in a given year, the assessed value is multiplied by the mill levy.³⁶ It does not matter what the tax rate is for a taxing district in a given year so long as that rate is applied equally to all property within the district.

WHEN ARE REAL PROPERTY TAXES DUE AND PAYABLE IN KANSAS

In Kansas, taxpayers can either pay the entire amount of tax on their real property on or before December 20 of each year, or pay half of the amount on December 20 and pay the second half on or before May 10 of the following year.³⁷ If a taxpayer has not paid at least half of his taxes on real property for the year by December 20, then interest accrues on the first half of the taxes at a rate prescribed by K.S.A. 79-4521 and may be paid before May 10 of the following year.³⁸ If the taxpayer has not paid the entire amount of tax due on his real property by May 11 of the following year, then interest accrues on the remaining amount owed at a rate prescribed by K.S.A. 79-4521 until it is fully paid.³⁹

ONE CONCERN WITH THE CURRENT PROPERTY TAX PAYMENT SYTEM

Although taxpayers have the option to pay only half of their taxes due on their real property in given year on or before December 20, this option does not do enough to protect taxpayers whose real property taxes dramatically increase from year to year. If for instance, the

value of a taxpayer's property significantly increases from one year to the next, the taxpayer will be required to pay the entire amount of his taxes before May 11 of the following year even if the amount is more than he is able to pay. This is a heavy burden on taxpayers who see their real property taxes increase dramatically from year to year. The current property tax payment system in Kansas only allows taxpayers to defer half of their taxes due for a couple of months before they must come up with the total amount. Although in theory this seems like a viable alternative to paying the entire amount of taxes due on a given date, it may not do enough to protect real property owners from dramatic spikes in the market from year to year.

HB 2769: AN ALTERNATIVE TO KANSAS'S PROPERTY TAX PAYMENT SYSTEM

WHAT DOES THE PROPERTY TAX AVERAGING PAYMENT PLAN DO?

HB 2769 would allow qualified taxpayers to enter into a property tax averaging payment plan over the course of several years. To qualify for the plan, the property must: be the homestead of the taxpayer; be owned or jointly owned by the taxpayer; be insured by a property and casualty insurance policy; not be income producing; and be free from all liens for taxes in previous years. If a taxpayer has been appointed a guardian, conservator, or attorney-in-fact, then the appointed person may act on the taxpayer's behalf in participating in the plan. The payment plan would have the effect of substituting the taxpayer's real property taxes due with a calculated amount based on the average tax due on the property for the years in which the taxpayer has participated in the plan, deferring the payment of part of the property's taxes for the years in which the taxpayer participates in the plan if the taxes calculated are less than the taxes due on the property in the current year, and creating a lien for such deferred taxes. Interest will accrue on the deferred taxes at a rate provided by K.S.A. 79-2968.

However, this is not a retroactive payment plan. Thus, the average payments on the taxed property will only be based off of the years in which the taxpayer participates in the plan.

Taxpayers will be required to pay the full amount of taxes due on the property for the first year of their plan. In the second year of the plan, taxpayers will be required to pay the average of the taxes due in that year and the previous year. In the third year of the plan, taxpayers will be required to pay the average of the taxes due in that year and the previous two years. The payment plan will continue until the taxpayer notifies the county treasurer to remove the property from the plan or if: the taxpayer dies; the property is sold or title is transferred to someone else; the property is no longer the homestead of the taxpayer; or the property becomes income producing.

Taxpayers participating in the plan must pay the amount calculated for a taxable year even if the plan results in a payment that is higher or lower than the property's taxes due in that year. If the calculated amount is higher than the taxes due in the current year, the county must first apply any excess amount to remove any liens placed on the property for underpayment of taxes in prior years due to participation in the plan. If there is any remaining amount, it must be remitted to the property tax averaging stabilization fund.

All deferred taxes, including accrued interest, becomes payable when: the taxpayer elects to remove the property from the plan; the taxpayer dies; the property is sold; the property is no longer the homestead of the taxpayer; or the property becomes income producing. Whenever any of these circumstances occurs, the property may not continue to participate in the payment plan until all unpaid taxes, including previously deferred taxes and accrued interest, have been paid. All deferred taxes and accrued interest becomes due and payable 90 days after the circumstance occurs. However, if a taxpayer dies, the deferred amount becomes due and payable 180 days after the taxpayer's death.

If a participating taxpayer becomes ill or dies, a spouse may elect to continue the property in the payment plan. If a spouse elects to continue participating in the plan, the spouse must apply for the payment plan with the county treasurer within 90 days. Once the spouse's application is filed and approved, the county and state treasurer must withdraw any action taken against the property. The spouse may continue the property in the payment plan as long as the property continues to be eligible for the plan.

WHAT ARE THE BENEFITS OF A TAX AVERAGING PAYMENT PLAN?

The tax averaging payment plan would allow homeowners who qualify for the plan to pay a calculated amount rather than their actual taxes due on their home in a given year. On the other hand, homeowners who elect not to participate in the plan would be required to pay their actual taxes due every year, i.e., the assessed value of the property multiplied by the mill levy rate. The payment plan would not change the way in which property taxes are computed, but it would change how much a participating taxpayer is required to pay in a given year by averaging the taxes due in the current year with those due in the previous years in which the homeowner participated in the plan and creating a lien on the deferred taxes with accruing interest.

Because participating homeowners are only required to pay the average calculated amount rather than their actual taxes due on their home every year, participating homeowners will be able to handle dramatic increases in property taxes from year to year. If there is a dramatic increase in property taxes from one year to the next, non-participating property taxpayers will be required to pay the full amount of their taxes by May 11 of the following year. On the other hand, participating taxpayers will only be required to pay the average calculated amount, and defer a part of their taxes to a later date. This gives participants a reliable cushion

that will lessen the burden of paying a dramatic increase in property taxes from year to year. Although the deferred taxes will become payable at some point in the future, the averaging plan offsets spikes in the market in a given year and allows taxpayers to pay off their property taxes over several years.

CONCERNS WITH THE PROPERTY TAX AVERAGING PAYMENT PLAN

REVENUE & BUDGETARY CONCERNS

Although the payment plan would protect homeowners from increases in property taxes from year to year, the payment plan will dramatically affect the generation of revenue for the counties and State. Because homeowners will be able to defer part of their payment in the years in which they participate in the plan, taxing districts will not receive the full amount of revenue from property taxes each year. Instead, the taxing districts will only receive the calculated amount of taxes due from participating homeowners. However, this is only temporary because the taxes will become due at some point in the future. The delay in the collection of property taxes will be offset by the accruing interest on the deferred taxes. Yet the plan does not place any time limitations for participation and it is unknown how long it will take for taxing districts to receive the entire amount of deferred taxes.

There are two state funds that are directly affected by this plan: the Education Building Fund (EBF) and the State Institutions Building Fund (SIBF).⁴⁰ The House Committee on Taxation estimates that if 10% of homeowners participate in the plan starting in 2016, then the plan would decrease revenue to these two funds by \$40,000 in FY 2017, with a \$26,667 loss to the EBF and a \$13,333 loss to the SIBF.⁴¹ The loss in property tax revenue would also affect state expenses for aid to school districts.⁴² The Department of Revenue estimates that state

expenditures for aid to schools will increase by \$510,000 in FY 2017.⁴³ The plan would also increase expenditures for counties in relation to approving and administering payment plans within their taxing districts.⁴⁴

The payment plan will also affect the mill levy rate for each taxing district. The mill levy rate is determined by a function of two things: the total amount of dollars the county has budgeted for property tax revenues and the total assessed valuation in the taxing district.⁴⁵ Because the mill levy rate is determined in part by the budgetary needs of the taxing district, the plan creates uncertainty in determining the budget for a given year. Once the mill levy rate is set, the districts budget is also set. Because of the averaging plan, the districts may not receive enough revenue for their budgetary needs. The districts must either anticipate this lack of revenue because of the plan and implement a higher mill levy rate, or trim down their budget so that the revenue generated is enough to cover it.

CONSTITUTIONAL CONCERNS

The payment plan could potentially violate Article XI of the Kansas Constitution because it could cause a disparity between participants and non-participants. There are two classes of taxpayers who could argue that their property is not being taxed in a uniform and equal manner in relation to participating taxpayers: homeowners within the same taxing district as a participant who elect not to participate in the payment plan and residential property owners within the same taxing district as a participant who may not participate in the payment plan. However, because eligible non-participants have the option to enter into the plan, it seems that this ability makes the plan uniform and equal as to all qualifying homeowners. In theory, any homeowner could make the election, so all are treated equally.

Residential property owners within the same taxing district may not be taxed in a uniform and equal manner because of the payment plan. The real property subclass of residential property owners includes property owners other than homeowners. However, homeowners are the only members of this subclass that are permitted to enter into the payment plan. Thus, the non-participating residential property owner is required to pay his actual taxes due on his property every year. That is, the assessed value of the property multiplied by the mill levy rate. Because the residential owner is not permitted to participate in the payment plan, he will always be required to pay his actual taxes due on his house every year. On the other hand, the participating homeowner is required to pay the calculated amount under the payment plan even if that amount differs from his actual taxes due on his home in a given year. Averaging the taxes in a given year with the taxes due in previous years results in a calculated amount that is different than the actual taxes due in a given year.

If the calculated amount is less than the participant's actual taxes in a given year, then a lien is created with interest and the remaining amount is deferred to a later date. Thus, participating homeowners are permitted to pay an amount of their tax in a given year that is different than non-participating homeowners. Non-participants' homes may not be taxed in a uniform or equal manner in relation to participants' homes. This disparate treatment between participants' and non-participants' taxes in a given year is the direct result of the payment plan.

The payment plan does not change how property taxes are calculated, but it would change how much a participant is required to pay in a given year by averaging the taxes on the property in the current year with those due in the previous years in which the property participates in the plan. Thus, participants' and nonparticipants' residential property must still be appraised at their fair market value in accordance with Kansas law. All property within the

subclass of residential property is subject to an assessment rate of 11½%. The taxing district must apply the same mill levy rate to each property. However, under the plan, participants are required to pay the averaged calculated amount while non-participants are required to pay their actual taxes due on their property each year.

Although the payment plan will have the effect of substituting the actual taxes a homeowner must pay in a given year with a calculated amount, it will also create a lien on the portion of the actual taxes that have not yet been paid. If a homeowner no longer wants to participate in the plan, or if he dies, the property is sold, the property is no longer the homestead of the owner, or the property becomes income producing, then the remaining taxes that have been deferred become payable by a specified date. Even though participants are required to pay an amount of their taxes that is different than non-participants, that does not mean that participants are being taxed at a different rate than non-participants. The Kansas Constitution does not require all property to be taxed the same amount; it only requires all property to be taxed in a uniform and equal manner.

The only thing the payment plan changes in relation to participants' actual taxes on their homes is when those taxes must be paid. Participants' taxes are only being deferred, not abated. Eventually participants will be required to pay all of the deferred taxes plus accrued interest for the years in which they participated in the plan. The plan does not provide a different rate of taxation for participants; it only provides an extended timeline in which participants' taxes will be paid. Thus, in the long run participants and non-participants are required to pay the same amount of total tax in relation to their property, but homeowners have a deferral advantage over other residential property owners. The payment plan offsets this advantage by requiring participants to pay interest on their deferred taxes. As long as the interest accrued is a

satisfactory measure of the time value of money, participants and non-participants will be taxed in a uniform and equal manner.

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- ¹ Kan. Const. Art. XI, § 1(a); Kan. Stat. Ann. § 79-101 (1997).
- ² Kan. Const. Art. XI, § 1; *Gunkle v. Killingsworth*, 233 P. 803, 804-805 (Kan. 1925).
- ³ Kan. Const. Art. XI, § 1(a).
- ⁴ *Black's Law Dictionary* (9th ed. 2009), property.
- ⁵ *Id.*
- ⁶ Kan. Const. Art. XI, §1(a).
- ⁷ *Id.*
- ⁸ *Id.*
- ⁹ *Addington v. Board of County Commissioners*, 382 P. 2d 315, 319 (Kan. 1963).
- ¹⁰ *Id.*
- ¹¹ *Id.*
- ¹² *In re City of Wichita*, 59 P.3d 336, 341 (Kan. 2002).
- ¹³ *Id.*
- ¹⁴ *Addington*, 382 P.2d at 319.
- ¹⁵ *Id.*
- ¹⁶ *Id.*
- ¹⁷ *Id.*
- ¹⁸ *Id.*
- ¹⁹ K.S.A. 19-428; K.S.A. 79-1455.
- ²⁰ Kan. Dept. of Rev., A Homeowner's Guide to Property Tax in Kansas.
- ²¹ K.S.A. 79-501.
- ²² K.S.A. 79-503a.
- ²³ *Id.*
- ²⁴ *In re Tax Appeal of Andrews*, 851 P.2d 1027, 1032 (Kan. 1993).
- ²⁵ Kan. Dept. of Rev., A Homeowner's Guide to Property Taxes in Kansas.
- ²⁶ *Id.*
- ²⁷ *Id.*
- ²⁸ *Id.*
- ²⁹ *Appeal of Andrews*, 851 P.2d at 1033.
- ³⁰ Kan. Dept. of Rev., A Homeowner's Guide to Property Taxes in Kansas.
- ³¹ Kan. Const. Art. XI, § 1(a).
- ³² Kan. Dept. of Rev., A Homeowner's Guide to Property Taxes in Kansas.
- ³³ *Id.*
- ³⁴ Gage A. Rolf, *Kansas Property Tax Appeals: An Adversarial System Without Adversaries*, 49 Washburn L.J. 871, 877 (2010).
- ³⁵ Kan. Const. Art. XI, §1(a).
- ³⁶ Kan. Dept. of Rev., A Homeowner's Guide to Property Taxes in Kansas.
- ³⁷ K.S.A. 79-2004.
- ³⁸ *Id.*
- ³⁹ *Id.*
- ⁴⁰ Fiscal Note for HB 2769
- ⁴¹ *Id.*
- ⁴² *Id.*

⁴³ *Id.*

⁴⁴ *Id.*

⁴⁵ K.S.A. 79-5A27; K.S.A. 79-1803; Gage A. Rolf, *Kansas Property Tax Appeals: An Adversarial System Without Adversaries*, 49 Washburn L.J. 871, 877 (2010).