



A REPORT
TO THE
MONTANA
LEGISLATURE

PERFORMANCE AUDIT

Property Tax Relief

Department of Revenue

AUGUST 2014

LEGISLATIVE AUDIT
DIVISION

14P-02

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PERFORMANCE AUDITS

Performance audits conducted by the Legislative Audit Division are designed to assess state government operations. From the audit work, a determination is made as to whether agencies and programs are accomplishing their purposes, and whether they can do so with greater efficiency and economy.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Members of the performance audit staff hold degrees in disciplines appropriate to the audit process.

Performance audits are performed at the request of the Legislative Audit Committee which is a bicameral and bipartisan standing committee of the Montana Legislature. The committee consists of six members of the Senate and six members of the House of Representatives.

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August 2014

The Legislative Audit Committee
of the Montana State Legislature:

This is our performance audit of the Property Tax Assistance Program, the Disabled American Veterans Exemption, and the Elderly Homeowner/Renter Program managed by the Department of Revenue (department). This report provides the legislature information about how the department administers property tax relief through these programs. This report includes recommendations for improving how these programs verify qualifying criteria and ensure that taxpayers only receive relief based on statutory guidance. This report also includes information regarding the overall distribution of property tax relief in the state, including if taxpayers are accessing multiple property tax relief programs offered by the department. A written response from the department is included at the end of the report.

We wish to express our appreciation to department personnel for their cooperation and assistance during the audit.

Respectfully submitted,

/s/ Tori Hunthausen

Tori Hunthausen, CPA
Legislative Auditor

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 MONTANA LEGISLATIVE AUDIT DIVISION

 PERFORMANCE AUDIT
 Property Tax Relief
 Department of Revenue

AUGUST 2014

14P-02

REPORT SUMMARY

The Department of Revenue administers various property tax relief programs that provide approximately \$20 million in annual benefits to taxpayers; we found weaknesses in the Department of Revenue procedures that resulted in some ineligible taxpayers receiving benefits, while some others received benefits in excess of statutory income and property ownership thresholds. The Department of Revenue should implement changes to ensure property tax relief benefits are administered consistently and also assess the distribution of benefits across the state.

Context

In Montana, there are four programs administered by the Department of Revenue (department) that provide residential property tax relief to individual taxpayers, including the Property Tax Assistance Program (PTAP), the Extended Property Tax Assistance Program (EPTAP), the Disabled American Veterans (DAV) Exemption, and the Elderly Home Owner/Renter Credit (elderly credit). The PTAP, EPTAP, and DAV programs target homeowners and ultimately reduce taxes through a reduction in the taxable value for properties that meet certain criterion. The elderly credit provides an income tax credit for elderly homeowners and renters based on property taxes and rent paid. According to department information, property tax relief programs provided a collective tax benefit of over \$20 million to individual taxpayers in 2012. State law outlines various eligibility requirements for property tax relief programs in the state with thresholds for eligible land and improvements, including factors such as income, age, veteran's disability status, and occupancy.

Audit work examined if the department has controls in place to verify eligibility requirements, to correctly calculate relief based on statutory thresholds for property

and income, and to examine how relief is used and distributed across the state. Audit work determined the department could improve how it verifies applicant eligibility requirements and ensures that relief benefits are calculated on a consistent basis. For example, we noted that it appears individual taxpayers are misreporting income as part of the determination process. Based on income misreporting, we identified approximately \$23,000 in benefits claimed in error by individual taxpayers. As a part of our work, we also concluded the various property tax relief programs administered by the department could be better coordinated. We determined the department should assess their outreach efforts to examine the distribution of benefits statewide.

Results

Audit recommendations address the need for the department to improve how it verifies applicant eligibility, calculates relief benefits, and assesses relief distribution across the state. Audit work also concludes the multiple property tax relief programs administered by the department are fragmented and uncoordinated. Recommendations and conclusions include:

(continued on back)

- ◆ Develop and implement management tools to verify occupancy requirements.
- ◆ Develop and implement management tools to verify income requirements and investigate ways to simplify income determinations.
- ◆ Develop and implement a quality control process to ensure taxpayers only receive relief on eligible property and investigate ways to automate the property calculation process.
- ◆ Develop and implement a quality control process to ensure taxpayers only receive relief based on qualifying income and investigate ways to automate the income calculation process.
- ◆ Examine outreach efforts to assess the distribution of relief benefits statewide.

Recommendation Concurrence	
Concur	5
Partially Concur	0
Do Not Concur	0
Source: Agency audit response included in final report.	

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Chapter I – Introduction

Introduction

Property taxes are generally defined as an annual local government tax on real property based on a tax rate established by a legislature. In Montana, while property taxes are calculated, billed, and collected by local taxing jurisdictions, the Department of Revenue (department) is responsible for ensuring that all property is treated equitably. The department's duties include the appraisal, assessment, and equalization of the value of all property in the state for the purpose of taxation. According to a past study of property tax relief conducted by the National Conference of State Legislatures, the property tax traditionally has been unpopular and is viewed as unfair by many taxpayers. This is particularly true for older Americans, who frequently live on fixed incomes and own their homes. As a result of taxpayer dissatisfaction, many states have implemented various property tax relief measures to alleviate the property tax burden. Although some of these tax relief programs are open to the general population, some limit participation to senior citizens and other targeted groups such as veterans or the disabled.

In Montana, there are four programs administered by the department which provide residential property tax relief to individual taxpayers, including the Property Tax Assistance Program (PTAP), the Extended Property Tax Assistance Program (EPTAP), the Disabled American Veterans (DAV) Exemption, and the Elderly Home Owner/Renter Credit (elderly credit). The PTAP, EPTAP, and DAV programs target homeowners and ultimately reduce taxes through a reduction in the taxable value for properties that meet certain criterion. The elderly credit provides an income tax credit for elderly homeowners and renters based on property taxes and rent paid. During the course of audit work, the department changed the name of DAV to the Montana Disabled Veteran Property Tax Relief program. However, in this report, we refer to the program as it was named during the period of our audit examination. Based on legislative interest in property tax relief, the Legislative Audit Committee identified a performance audit of these programs as a priority. This chapter discusses the scope of our audit work and provides background information on how these various relief programs are administered by the department, including areas within the department where we conducted audit work.

Audit Objectives

During our assessment work, we determined audit work should focus primarily on how the department administers the PTAP and DAV programs, due in large part to the fact that activities for these two programs are decentralized and administered by department field staff in each of Montana's 56 counties. We also determined the

geographic distribution of Montana's four property tax relief programs should be examined to determine how the programs are utilized by property taxpayers in the state. As a result, we developed three objectives for examining how the department manages program activities. Our audit work answered the following three questions:

- ◆ Does the department have effective controls in place to verify the eligibility of PTAP and DAV applicants based on the program requirements outlined in applicable state law, administrative rules, and policies and procedures?
- ◆ Does the department appropriately calculate the reduction of the residential class 4 tax rate based on applicant income and program thresholds for eligible land and property improvements?
- ◆ How is property tax relief used and distributed across the state by Montana taxpayers?

Audit Scope and Methodologies

Due to the fact that there are several property tax relief programs administered by the department, during our assessment work we reviewed how the department manages these various programs in order to determine where to focus our audit efforts. The four programs which provide property tax relief to individual taxpayers are managed by two department divisions, namely the Property Assessment Division (PAD) and Business and Income Taxes Division (BITD). PTAP, EPTAP and DAV are managed by PAD, while the elderly credit program is administered by BITD. PAD is responsible for administering Montana's property tax laws, including the valuation and assessment of real and personal property throughout the state for property tax purposes. BITD is responsible for the administration, compliance, collection and valuation of approximately 30 tax types, including corporation income, individual income, withholding taxes, and various natural resource taxes.

During our assessment work, we determined there were risks associated with PTAP and DAV. Assessment work indicated the statutory basis for both PTAP and DAV are complex, with numerous tiers of eligibility, with limitations based on income and property. Due to the fact that EPTAP is centrally administered and focuses only on residential properties which have experienced extraordinary market value increases between 2002 and 2008, as a result of the most recent reappraisal cycle, we generally excluded EPTAP from the scope of our examination. Overall, our audit work examined how the department verifies eligibility requirements and calculates property tax reductions for PTAP and DAV. Our audit work also examined how relief is distributed geographically for the elderly credit, including the extent to which individual taxpayers are using multiple programs to obtain property tax relief. To accomplish our objectives, we completed the following methodologies:

- ◆ Reviewed applicable state laws, administrative rules, and program policies for property tax relief programs administered by the department.
- ◆ Reviewed a sample of department hardcopy files for granted PTAP and DAV applicants from the 2013 tax year in the five counties in Montana with the highest combined number of granted applicants—namely Yellowstone, Missoula, Cascade, Flathead, and Ravalli counties—in order to test income, occupancy, and disability documentation controls, for a total of 200 combined PTAP and DAV granted applications.
- ◆ Obtained and reviewed real estate transaction data from the department’s Orion database for all—17,035 PTAP and 2,015 DAV—granted applicants in 2013 to determine if the property for which a taxpayer received relief was occupied in the last six months of 2012.
- ◆ Obtained and reviewed available individual income tax data for all PTAP and DAV granted applicants in 2013 to compare income reported as part of individual income taxes with income reported by individuals as part of the property tax relief application process.
- ◆ Obtained and reviewed property tax relief data from the department’s Orion database for all PTAP and DAV granted applicants in 2013 to determine if individual taxpayers are receiving the appropriate property tax relief based on qualifying income and thresholds for eligible property.
- ◆ Obtained and reviewed available department data for all individuals who received the elderly credit in 2012 to determine how the credit was distributed geographically across the state relative to PTAP, EPTAP, and DAV in 2012 and the extent to which taxpayers are using multiple property tax relief programs.
- ◆ Interviewed department staff in Helena and in five of the departments’ local field offices to discuss how property tax relief programs are administered, including verifying eligibility, calculating tax rate reductions, and coordinating with other relief activities.
- ◆ Obtained and reviewed information for property tax relief activities, including interviews, in other states to assess how other states administer similar activities, such as verifying eligibility, calculating tax rate reductions, and coordinating with other relief activities.

Montana Property Tax Relief Program Landscape

In the realm of property taxes, Montana is one of only two states that centrally administer property values for the purpose of taxation. The majority of other states assess property values at the level of local government. Similarly, property tax relief programs in other states are primarily administered by local government, rather than administered by a state taxation agency, as is the case in Montana. And while the four programs administered by the department share overall similarities to provide property tax relief, the intent and eligibility requirements are unique and differ between each program, as is also the case in other states. To some extent, each of the programs in

Montana targets relief to a specific population, including senior citizens, individuals with low incomes, and disabled veterans. Individual taxpayers may apply for multiple programs to maximize the amount of relief they may receive, as long as they meet the specific eligibility requirements for each program. Each of these programs also has similar but unique limitations on the type of property and amount of land for which relief may be obtained, such as the primary residential dwelling and the appurtenant land. Between PTAP, EPTAP, DAV, and the elderly credit, property tax relief programs provided a collective tax benefit of over \$20 million to individual tax payers in the 2012 tax year.

Table 1
2012 Total Tax Benefits for Property Tax Relief Programs

Program Name	Program Benefits
Elderly Homeowner/Renter Credit	\$ 9,641,545
Property Tax Assistance Program	7,673,698
Disabled American Veterans Exemption	2,458,900
Extended Property Tax Assistance Program	820,993
Total	\$20,595,136

Source: Compiled by the Legislative Audit Division from department records.

Table 1 summarizes the total tax benefit in 2012 for the four residential property tax relief programs administered by the department.

Property tax relief available through PTAP, EPTAP, and DAV most directly impacts the operational

revenue of local government as a result of a reduction in the tax rate applied to a property's taxable market value and has little if any direct impact on the operations of state government. However, property tax relief available through the elderly credit impacts the state directly, as this program is administered as an income tax credit and results in a reduction to the state's general fund. Table 2 on page 5 briefly summarizes the key characteristics of the three property tax relief programs we examined over the course of our audit, including PTAP, DAV, and the elderly credit.

Table 2
2013 Key Eligibility Characteristics for Property Tax Relief Program

Program Name	Target Audience	Age Requirement	Income Requirement	Land Limit	Occupancy Requirement	Maximum Benefit
Property Tax Assistance Program	Low Income	NA	Less than \$27,745	5 acres	7 months	NA
Disabled American Veterans Exemption	Disabled veterans or surviving spouses	NA	Less than \$55,229	5 acres	7 months	NA
The Elderly Homeowner/Renter Credit	Elderly	62	Less than \$45,000	1 acre	6 months	\$1,000

Source: Compiled by the Legislative Audit Division from department records.

The Property Tax Assistance Program

The Property Tax Assistance Program—or PTAP—is a property tax relief program that provides relief to low-income households. Section 15-6-134, MCA, outlines the program’s requirements. Additional program requirements are outlined in administrative rules. Per state law, the program provides relief on an annual basis on the first \$100,000 or less of the taxable market value of any improvement on real property, including trailers, manufactured homes, or mobile homes, and appurtenant land not exceeding 5 acres owned and occupied as the primary residential dwelling of one or more qualified claimants. Taxable market value refers to the portion of the property’s assessed value which is used to determine the property’s taxable value. Property qualifying for the program is taxed at a rate defined in state law—2.54 percent in 2013—of its taxable market value multiplied by a percentage figure based on the income for the preceding calendar year of the owner or owners who occupied the property as their primary residence. Qualifying income for the program is adjusted for inflation annually by the department. According to the department’s 2010-2012 Biennial Report, in 2012 the estimated tax benefit provided by PTAP to participants was \$7,673,698 for 14,013 participants. PTAP is regionally administered by the PAD, which was budgeted \$41,178,601 for the 2015 biennium with a full-time equivalent (FTE) of 311.35. Appendix A provides a table of the distribution of PTAP in Montana’s 56 counties in 2013.

The Disabled American Veterans Exemption

The Disabled American Veterans’ Exemption—or DAV—provides property tax relief on an annual basis for a residence and appurtenant land, not to exceed 5 acres, on which it is built that is owned and occupied by a veteran or a veteran’s spouse. There

is no limit on the taxable market value of any improvement on real property for DAV. Section 15-6-211, MCA, outlines the program's requirements. Additional program requirements are outlined in administrative rules. According to the law, the exemption is available for a veteran currently rated 100 percent disabled by the U.S. Department of Veterans Affairs for a service-connected disability or their surviving spouse. Property qualifying for the program is taxed at a rate defined in state law—2.54 percent in 2013—of its taxable market value multiplied by a percentage figure based on the income for the preceding calendar year of the owner or owners who occupied the property as their primary residence. Qualifying income for the program is adjusted for inflation annually by the department. According to the department's 2010-2012 Biennial Report, in 2012, the estimated tax benefit provided by DAV to participants was \$2,458,900 for 2,095 participants. DAV is administered regionally by PAD. Appendix A provides a table of the distribution of DAV in Montana's 56 counties in 2013.

The Elderly Home Owner/Renter Credit

Sections 15-30-2337 - 2341, MCA, provide for a residential property tax credit available for the elderly commonly referred to as the Elderly Home Owner/Renter Credit. Additional program requirements are outlined in administrative rules. The elderly credit is an income tax credit available to qualifying taxpayers based on household income adjusted by the amount of property taxes, fees, special assessments and special improvement districts billed on a residence and land not to exceed one acre. State law outlines qualifying criteria for the credit, including a reduction schedule based on property tax billed or rent-equivalent tax paid. The credit is essentially a property tax refund administered through the income tax system. Taxpayers pay their property taxes and have part refunded via an income tax credit which reduces revenue to the state general fund. For taxpayers who rent, the credit subsidizes the rent they pay. According to department data, in 2012 the total tax benefit provided by the elderly credit to participants was \$9,641,545 from the state general fund for 20,324 participants. The elderly credit is administered centrally by the BITD, which was budgeted \$19,524,219 for the 2015 biennium with an FTE of 138.45.

Report Contents

The remainder of this report includes chapters detailing our findings, conclusions, and recommendations in the following areas:

- ◆ Chapter II discusses how the department should verify program eligibility requirements, including occupancy and income.
- ◆ Chapter III addresses how the department should ensure that qualified applicants are receiving the appropriate benefit based on income and property thresholds.
- ◆ Chapter IV discusses the various property tax relief options available and the department's responsibility to actively assess their property tax relief outreach efforts in the state.

Chapter II – Verifying Eligibility Requirements

Introduction

Our first audit objective examined how the Department of Revenue (department) verifies the eligibility of taxpayers who apply for the Property Tax Assistance Program (PTAP) and the Disabled American Veterans (DAV) Exemption. The department's Property Assessment Division (PAD) is responsible for the administration of both PTAP and DAV. While management for the two programs is centrally located in Helena, PAD has a local office in the seat of each of Montana's 56 counties where field staff receive, review, and approve taxpayer program applications. Both PTAP and DAV are available to qualified owners on their primary residential dwelling. To qualify for either PTAP or DAV, taxpayers must meet a number of eligibility requirements. As part of our audit work, we determined the department could improve how it verifies the eligibility of PTAP and DAV applicants based on applicable program requirements, including terms of occupancy and income thresholds. This chapter provides information on eligibility requirements and discusses our findings and recommendations related to improving how the department verifies eligibility requirements.

State Law Outlines Occupancy and Income Requirements

While PTAP and DAV may target different populations, they share a number of similarities, including expectations that the taxpayers applying for relief occupy the residence as their primary dwelling. For PTAP, §15-6-134 (1)(c), MCA, states in part the residence must be owned and actually occupied for at least seven months a year as the primary residential dwelling of one or more qualified claimants. As for DAV, §15-6-211 (1), MCA, states in part that a residence owned and occupied by a veteran or a veteran's spouse is exempt from property taxation. While the law for DAV requires the eligible property be owned and occupied by a veteran or a veteran's spouse, there is no specific term of occupancy outlined in the law for DAV as with PTAP. For DAV, ARM 42.19.501 (9) indicates exemption is for a residence which is occupied for more than seven months annually. However, for DAV, ARM 42.19.501 (12)(a) states that a qualified applicant will receive the exemption if they apply by the deadline. Nonetheless, while the law for DAV does not specify a term of occupancy, it is clear that was the intention of the legislature to provide the exemption to qualified applicants for owned and occupied residential properties. Based on statutory guidance, the department established a seven-month term of occupancy for DAV in administrative rules to mirror the PTAP requirement.

Both PTAP and DAV are income-based relief programs, with the amount of relief available to taxpayers determined by their annual income. Qualifying income for both programs is adjusted for inflation annually by the department. Section 15-6-134 (2)

Table 3
2013 Adjusted PTAP Qualifying Income and Reductions

Applicants Income		Percent Reduction
Single	Multiple or Head of Household	
\$ 0 - \$ 8,324	\$ 0 - \$11,098	80
\$ 8,325 - \$12,763	\$11,099 - \$19,422	50
\$12,764 - \$20,809	\$19,423 - \$27,745	30

Source: Compiled by the Legislative Audit Division from department records.

(b)(i), MCA, outlines income qualifications for PTAP. The taxable market value of property qualifying under PTAP is taxed at the rate determined by the legislature and subsequently multiplied by a percentage based on the income for the preceding calendar year. This results in a reduced tax rate for the qualifying taxpayer. Similarly, property qualifying for DAV is taxed at a rate determined by the legislature and subsequently

multiplied by a percent based on qualifying income. Section 15-6-211(2), MCA, outlines income qualifications for DAV. In 2013, the adjusted qualifying income and percentages of reduction for PTAP and DAV are as outlined in Table 3 and Table 4.

Table 4
2013 Adjusted DAV Qualifying Income and Reductions

Applicant's Income			Percent Reduction
Single	Multiple or Head of Household	Surviving Spouse	
\$ 0 - \$36,819	\$ 0 - \$44,183	\$ 0 - \$30,683	100
\$36,820 - \$40,501	\$44,184 - \$47,865	\$30,684 - \$34,365	80
\$40,502 - \$44,183	\$47,866 - \$51,547	\$34,366 - \$38,047	70
\$44,184 - \$47,865	\$51,548 - \$55,229	\$38,048 - \$41,729	50

Source: Compiled by the Legislative Audit Division from department records.

In 2013 the tax rate for residential property was 2.54 percent as set by state law. For taxpayers who exceeded the program's income threshold, they would be taxed at the full tax rate established by the legislature. However, with PTAP, taxpayers receive a reduction in the taxable value of their property based on a reduction in the tax rate, after a standard homestead exemption. The taxable value of a property would then be multiplied by the mill levy of a local jurisdiction to arrive at a taxpayer's property taxes. Table 5 on page 9 compares and illustrates the impact of PTAP on a single income taxpayer's taxable value in 2013.

Table 5
2013 Comparison of PTAP Benefit for a Single Income Taxpayer Based on Qualifying Income

Single Taxpayer	Income	Eligible	Taxable Market Value	2013 Tax Rate	Tax Rate Reduction Eligibility Based on Income	Reduced Tax Rate	Taxable Value
A	\$5,000	Yes	\$100,000	2.54%	80%	0.51%	\$510
B	\$10,000	Yes	\$100,000	2.54%	50%	1.27%	\$1,270
C	\$15,000	Yes	\$100,000	2.54%	30%	1.78%	\$1,780
D	\$25,000	No	\$100,000	2.54%	NA	NA	\$2,540

Source: Compiled by the Legislative Audit Division from department records.

Some Ineligible Taxpayers May Be Receiving Relief

As part of reviewing a taxpayer's PTAP or DAV application, the department will review ownership data within the department's Orion database to assess if a taxpayer owns the property for which they wish to obtain relief. Department staff also will review supporting documentation provided by an applicant to determine if a taxpayer appears to be occupying the property. For example, department staff will review mailing addresses on supporting documentation to ensure it is the same address as the property for which relief is being sought. For the most part, these activities provide an adequate level of verification to ensure a taxpayer is occupying the property. However, there are taxpayers who are receiving relief who do not meet program occupancy requirements. During the course of audit work, we reviewed electronic data for 17,035 granted PTAP applicants and 2,015 granted DAV applicants for 2013. In order to assess if a taxpayer occupied the property for which they were applying for relief as their primary residence for at least seven months annually, we reviewed real estate transaction data and changes in ownership from the last six months of 2012 on those properties which were granted relief in 2013. It is important to note that ownership and occupancy are not the same thing. However, we used real estate transactions and changes in ownership to infer occupancy.

As part of our work, we determined there were individual taxpayers receiving property tax relief who did not actually occupy the property for at least seven months annually. We determined there were 23 PTAP applicants and 26 DAV applicants who did not occupy their properties for seven months based on real estate transaction data. For the 23 PTAP and 26 DAV granted applicants from 2013, we determined that if these individuals did not meet occupancy requirements it would result in approximately \$12,000 for PTAP and \$36,000 for DAV of property tax benefits granted in error to

individual taxpayers. For example, we noted one taxpayer who purchased a home in August of 2012 and received the PTAP benefit of over \$1,200 in 2013. In addition to ineligible individuals receiving benefits, local government is impacted, as these potential benefit errors represent a reduction in the operational revenue of local government which is primarily supported by the collection of property taxes.

The Department Could Improve Occupancy Verification

While the number of individuals we identified as part of audit work is minor relative to the number taxpayers who received benefits in 2013, there are additional ways in which the department could improve how it verifies occupancy. According to department staff, applicants for PTAP and DAV self-affirm occupancy requirements as part of their completed applications. Unless there is something which flags a reviewer's attention, such as an out-of-state address, the application is taken at face value and occupancy is infrequently investigated or verified. Department staff reported they do not have the time or the resources to actively verify and investigate occupancy requirements. They stress ownership and occupancy are not the same thing and it would be unreasonable for the department to try to verify actual occupancy. They indicated the Orion data system which they use to administer PTAP and DAV will flag properties where there has been a real estate transfer on the property in the preceding year; however, the system does not prevent a staff reviewer from approving an application. Department staff acknowledged that a number of the PTAP individuals we identified represent taxpayers who received benefits in error. However, staff also reported that while several of these applicants were individuals who may have moved during the year, they still met the income requirements. Department staff described this as a technicality where the applicant met all the other eligibility requirements and they did not want to deny the applicant based on the fact they moved. However, state law and administrative rules are clear in regard to applicants: they must both own and occupy the property for which relief is sought for at least seven months annually. The department may choose to pursue statutory changes to address these types of circumstances, if they believe the law unfairly excludes eligible applicants. During the course of audit work, department staff indicated while they are unable to verify all circumstances of occupancy, they plan to develop additional management tools to identify those individuals who clearly do not meet occupancy requirements based on change in property ownership.

RECOMMENDATION #1

We recommend the department develop and implement additional management tools to improve how they verify the occupancy requirements of the Property Tax Assistance Program.

Property Tax Relief Is Based on Income

As part of the PTAP and DAV application process, individual taxpayers are required to provide supporting income documentation which is used to determine the percentage of relief which a taxpayer may obtain on eligible property. However, how income is defined differs between PTAP and DAV. PTAP is based on total household income, while DAV is based on federal adjusted gross income. For the purposes of determining income, state law for PTAP defines total household income as the income as reported on the tax return or returns, excluding losses, depletion, and depreciation and before any federal or state adjustments to income. For DAV, federal adjusted gross income is defined as the taxpayer's income for the preceding calendar year, as reported on the taxpayer's federal income tax return. For PTAP, a taxpayer will provide a copy of their Montana individual income tax return, while for DAV a taxpayer will provide a copy of their federal income tax return. For those taxpayers who are not required to file an income tax return, they provide other supporting evidence of income, such as a social security statement, a W-2, or interest earning statements. As part of the application process, department staff will review income documentation and make a determination of the taxpayer's reportable income and ultimately the level of relief for which they are eligible.

The Department Generally Reviews Supporting Income Documentation

As part of our audit work, we traveled to the five counties in Montana with the combined highest number of granted applicants for PTAP and DAV in 2013 to review a total sample of 200 relief applications and supporting income documentation and discuss the income determination process with field staff. The five counties we visited included Yellowstone, Missoula, Cascade, Flathead, and Ravalli. Table 6 on page 12 represents the number of granted applicants in these counties in 2013, which formed the basis of our review sample.

Table 6
Top Five Granted Applicant Counties Sampled For PTAP and DAV in 2013

County	PTAP	DAV	Total	Sample
Yellowstone	2,051	221	2,272	40
Missoula	1,578	154	1,732	40
Cascade	1,461	268	1,729	40
Flathead	1,514	171	1,685	40
Ravalli	1,407	169	1,576	40
Total	8,011	983	8,994	200

Source: Compiled by the Legislative Audit Division from department records.

As part of our work, we determined that while income documentation was generally available for reviewed applications, there were inconsistencies regarding how field staff reviewed and interpreted supporting income documentation. There were circumstances in each of the field offices we visited where it was unclear how the staff reviewer arrived at the qualifying income determination and staff were unable to duplicate the income determination when requested. For example, there were PTAP applications where it appeared the staff reviewer did not exclude losses, depletion, or depreciation as required by the law. There were also DAV examples where it appeared the applicant had sources of income not included in the determination, such as rental property income. There were also PTAP examples where, based on the level of income reported, the applicant likely met the income threshold for being required to file in 2012, but the applicant did not provide a Montana tax return. Overall, the general manner in which field staff reviewed and interpreted income documentation was not clear or well documented.

Are Property Tax Relief Taxpayers Correctly Reporting Income?

As part of our audit work, we also reviewed income data housed within the department's Orion database for 17,035 granted PTAP applicants and 2,015 granted DAV applicants for 2013. In addition to reviewing income data housed in Orion, we obtained available individual income tax information from the department's Business and Income Tax Division (BITD) for those individuals who received a PTAP or DAV benefit in 2013 and filed an income tax return for 2012. Property tax relief determinations are based on a taxpayer's income from the previous year. We obtained this individual income tax information in an effort to compare the amount of income a taxpayer reported to PAD as part of the property tax relief process versus the amount of income a taxpayer reported to BITD staff as part of an individual income tax filing for those individuals

who filed a tax return for 2012. We were able to match approximately fifty percent of taxpayers based on identifiers such as names, addresses, and zip codes. Those taxpayers that we were unable to match presumably represented nonfilers or individuals who do not earn enough income requiring them to file an income tax return. However, there were some questions as to the integrity of those matches due to a difference in the format of the data between the two sources and the lack of a consistent common identifier. While it was not possible to easily identify all of those taxpayers who filed with BITD and received PTAP or DAV benefits in 2013 due to the lack of a consistent common identifier, we were able to compare the income between PAD and BITD for those individuals who reported a greater income to BITD than PAD and for whom a social security number was available from both sets of data. Based solely on social security numbers, we identified 223 taxpayers who received PTAP and 13 taxpayers who received DAV. For these taxpayers we noted significant discrepancies in the amount of income they had reported to PAD versus the amount of income that had been reported to BITD, including some cases where the level of income reported to BITD indicated they were not eligible to receive the PTAP or DAV benefit. As part of our work, we also calculated the benefit error based on the income reported to BITD. In total, for these individuals we identified above, we noted benefit errors for PTAP exceeded \$20,000, while benefit errors for DAV represented nearly \$3,000. Table 7 on page 14 represents ten selected examples of discrepancies in reported income between PAD and BITD for PTAP individuals for which we were able to match social security numbers, including the amount of income reported to PAD and BITD, the tax rate which would be applied to the taxable market value of their property based on that income, and the amount of benefit received in error by the taxpayer.

Table 7
2013 Selected Examples of Property Tax Assistance Program Income Disparities

Taxpayer	PAD Income	BITD Income	Tax Rate Based on PAD Income	Tax Rate Based on BITD Income	Benefit Error
A	\$4,743	\$76,406	0.51	2.54	\$1,287.90
B	\$921	\$77,632	0.51	2.54	\$1,110.52
C	\$11,725	\$26,875	0.51	2.54	\$1,073.99
D	\$8,278	\$39,773	0.51	2.54	\$1,064.20
E	\$1	\$128,491	0.51	2.54	\$943.91
F	\$2,394	\$40,435	0.51	2.54	\$868.25
G	\$8,220	\$17,938	0.51	1.78	\$640.61
H	\$15,155	\$28,178	1.78	2.54	\$382.81
I	\$9,790	\$12,000	0.51	1.27	\$324.56
J	\$6,920	\$11,975	0.51	1.27	\$246.68

Source: Compiled by Legislative Audit Division from department records.

While there may be some questions regarding the filing status or property ownership of the taxpayers we identified, the examples in Table 7 at a minimum generate concerns over whether taxpayers are honestly reporting their income to PAD as part of the relief determination process. Based on the potential for a taxpayer to fraudulently obtain property tax relief benefits, it would be in the best interest of the department to develop additional tools to verify income for PTAP and DAV applicants to ensure that relief benefits are being granted to taxpayers with limited income as intended by the legislature.

The Department Could Improve Qualifying Income Verification

According to department staff, supporting income documentation is not routinely investigated or verified and what an applicant provides is generally taken at face value by the reviewer. Staff indicate they have challenges within PAD to verify supporting income information. PAD staff indicate they generally do not verify reported income with BITD. PAD staff may consult with BITD staff, if they have a concern, but this is done infrequently. The department cites security concerns over PAD staff having access to individual income tax information which is the responsibility of BITD staff. The department has established guidance for staff to receive and process PTAP and DAV applications, including a running Q&A document which collects common and

unique scenarios submitted by field staff in order to help them consistently interpret income requirements for each program; however, based on audit work, it is clear that income determination is a frequent and ongoing concern for field staff who review and approve benefit applications. While these various resources provide field staff with direction on how to review and record application income information, income verification could be improved.

Other States Routinely Verify Qualifying Income

Relief programs in other states we reviewed as part of our audit work share similarities to PTAP and DAV, in terms of qualifying eligibility criteria, including income. However, we noted other states actively verify income information to ensure that only eligible taxpayers receive property tax relief. For example, in Idaho, with the Property Tax Reduction Program, which reduces property taxes for qualified applicants based on a number of qualifying criteria, income is verified for each applicant. In Idaho, the state directly reimburses local government for any property tax relief issued at the local level from the state's general fund. As such, after local government receives and reviews relief applications, all income documentation is submitted to the Idaho Tax Commission which verifies the income of each applicant in several ways, including cross-referencing income information with the state and federal individual income tax function. The state has also established reciprocal agreements with the Social Security Administration and the federal Department of Veterans' Affairs to verify social security and disability-related income. Montana could develop similar practices to ensure that only eligible taxpayers receive property tax relief in the state based on their qualifying income.

Could Income Determinations Be Simplified?

As part of our audit work, we discussed whether income determinations on the part of the department for PTAP and DAV could be simplified from both an administrative perspective and for the individual taxpayer. We discussed how PAD collects social security numbers as part of the relief applicant process, but staff do not routinely enter that information into Orion. Department staff report that income matching could be done between the PAD and BITD, but there would be timing issues regarding the availability of income information when relief applications are due. And for those taxpayers who are not required to file, income comparison between PAD and BITD would not be meaningful. Department staff also indicate the various programs can be confusing for taxpayers due to individual income eligibility requirements for each program. However, past legislative efforts to consolidate the various programs have been unsuccessful due to a perception that a change in programs will result in a reduction or loss of benefits for certain populations. Until changed by the legislature, both PTAP and DAV are income-based programs. While there may be issues to

address in the arena of income verification, it would be beneficial for the department to develop a means to simplify the income documentation required by an individual taxpayer and administrative burden placed on PAD to interpret income. Potential but not all inclusive courses of action available to the department include seeking statutory changes to existing income requirements, reducing the amount of documentation provided by taxpayers and verifying income based solely on social security numbers, or developing a means to effectively compare the income reported in PAD and BITD. During audit work, department staff indicated they are developing additional management tools to compare income in the short-term and discussing other potential long-term solutions to simplify income verification for property tax relief programs.

RECOMMENDATION #2

We recommend the department:

- A. *Develop and implement additional management tools to improve income verification between the Property Assessment Division and the Business and Income Tax Division for the Property Tax Assistance Program and the Disabled American Veteran's Exemption, and*
 - B. *Investigate ways to simplify income documentation provided by applicants for property tax relief programs administered by the department, including the Property Tax Assistance Program and the Disabled American Veteran's Exemption.*
-

Chapter III – Ensuring Relief Is Based On Qualifying Property And Income

Introduction

Our second audit objective examined how the Department of Revenue (department) calculates property tax reductions for the Property Tax Assistance Program (PTAP) and the Disabled American Veterans (DAV) Exemption. In contrast to other states, property tax relief is administered and relief calculated by a state agency, rather than by local government. The department's Property Assessment Division (PAD) is responsible for the administration of both PTAP and DAV. While management for the two programs is centrally located in Helena, PAD has a local county office in the seat of each of Montana's 56 counties where field staff receive, review, and approve taxpayer program applications. The amount of tax relief available for each program for eligible taxpayers is limited by property thresholds and income tiers outlined in state law. During our audit work, we determined that the department could establish additional practices to ensure relief benefits are calculated on a consistent basis. This chapter discusses thresholds for property and income and presents findings and recommendations for the department to ensure that qualified applicants receive the appropriate amount of relief.

State Law Outlines Eligible Property and Income Thresholds

Statutory guidance for PTAP and DAV place limits on the type and amount of property which is eligible for relief. Both PTAP and DAV target residential homeowners, including the households of low-income individuals and disabled veterans or their surviving spouses. And while there are similarities regarding the amount of eligible property for which a taxpayer may obtain relief, there are differences between the two programs. Section 15-6-134 (1)(c), MCA, indicates that PTAP relief is available on the first \$100,000 or less of the taxable market value of any improvement on real property, including trailers, manufactured homes, or mobile homes, and appurtenant land not exceeding 5 acres owned and occupied by a qualified taxpayer. Section 15-6-211 (1), MCA, provides that DAV may be applied to a residence and appurtenant land, not to exceed 5 acres that is owned and occupied by a veteran or a veteran's spouse. In contrast to PTAP, there is no limit for DAV regarding the amount of taxable market value for which relief is available. In the case of PTAP and DAV, the taxable market value refers to the portion of a property's assessed value which is subject to a tax rate established by the legislature. When considering a residence, both programs in practice allow for relief on a taxpayer's primary residence, including an attached or detached garage. And as discussed in the previous chapter, both PTAP and DAV are income-

based programs, with specific percentages of relief corresponding to a series of income tiers. The taxable market value of a qualified taxpayer's property is taxed at a rate determined by the legislature and then subsequently multiplied by a percentage based on the income from the preceding calendar year.

Some Taxpayers Are Receiving Relief Benefits on Ineligible Property

As part of our work reviewing data housed within Orion, the department's database used to administer property tax relief programs, we reviewed how the department calculated and applied relief on the property of qualified taxpayers. We reviewed data for 17,035 granted PTAP applicants and 2,015 granted DAV applicants in 2013. For PTAP, we reviewed department data to determine if qualified taxpayers were receiving relief on property in excess of \$100,000 in taxable market value. For both PTAP and DAV, we reviewed department data to determine if qualified taxpayers were receiving relief on more than 5 acres of land. As part of the relief determination process, department staff routinely must use a manual adjustment or apportionment process to apply relief only to eligible property. This manual process is completed outside of Orion on a spreadsheet tool developed by central staff in Helena. After completing this manual adjustment process, department staff will enter the appropriate information in Orion. Regarding benefits being applied in excess of \$100,000 of the taxable market value and taxpayers receiving relief on more than 5 acres, we identified numerous examples of taxpayers receiving relief on ineligible property. In total, we identified 525 individuals who received a PTAP benefit in excess of \$100,000 taxable market value of their property. We also identified 201 PTAP applicants and 27 DAV applicants who received a benefit on the value of more than 5 acres of land. The following bullets are examples of individual taxpayers receiving benefits on ineligible property which we identified during our work.

- ◆ A taxpayer received a PTAP benefit on \$151,051 of the taxable market value of their property. This resulted in an additional benefit of \$407.97 for this taxpayer.
- ◆ A taxpayer received a PTAP benefit on a land value of \$168,000 while they were eligible to receive a benefit on a land value of only \$60,000 or 5 acres of their land. This resulted in an additional benefit of \$743.57 for this taxpayer.
- ◆ A taxpayer received a DAV benefit on a land value of \$377,125 while they were eligible to receive a benefit on a land value of only \$215,500 or 5 acres of their land. This resulted in an additional benefit of \$940.19 for this taxpayer.

Local Government Operational Revenue Is Impacted

When taxpayers receive property tax relief on ineligible property, not only do those individuals receive a benefit in excess of what is appropriate, a financial reduction

in the operational revenue of local government occurs. According to department literature regarding the distribution of property taxes, over 80 percent of property taxes in Montana directly finance local government services and schools, while approximately 20 percent go to the state to equalize the funding of schools across the state. Local government is most directly impacted by the department calculating PTAP and DAV benefits incorrectly. As part of our work, we calculated the total excess benefits which occurred as result of taxpayers receiving benefits on ineligible property. We determined that the total excess benefit and impact to local government for PTAP benefits exceeding \$100,000 in taxable market value was more than \$7,000. We determined that the total excess benefit and impact to local government for PTAP and DAV combined for land value in excess of 5 acres totaled nearly \$19,000.

A Quality Control Process Could Improve That Only Eligible Property Receives Relief

According to department staff, they face a number of challenges to correctly calculate relief based on eligible property thresholds on a consistent basis for PTAP and DAV. They cite a complex process driven by a series of manual data entries in Orion by reviewing staff. They indicate there are limitations in Orion to calculate relief on property which exceeds limits in the law, which requires a manual adjustment or apportionment to apply relief only to eligible land and improvements as part of the relief determination process. As a result, the process can get complicated. Department staff indicated 363 of the PTAP exceeding \$100,000 errors we identified amounted to a dollar or two per individual due to rounding in Orion. They also reported, in regard to the excess land value for PTAP, in some cases there was no additional benefit provided to the taxpayer, as the reviewer had also incorrectly calculated the benefit for the property's improvements and did not exceed the \$100,000 limit in taxable market value for the benefit. According to staff, while the department has developed procedures for apportioning property, there currently is not a quality control process in place to ensure the determinations made by field staff are correct. Department staff indicated more automation in Orion may be a solution for eligible land, but may be challenging for improvements. However, they will investigate more automation solutions. During the course of our audit work, the department reported that in the short-term they are in the process of developing additional management tools to ensure taxpayers only receive relief on eligible property.

Other States Have Implemented a Quality Control Process

In contrast to Montana, relief determinations in the other states we reviewed are generally more of an automated process, without a manual adjustment or apportionment process for eligible property. For example, in Idaho, the Property Tax Reduction Program provides relief on an applicant's property taxes on their home up to 1 acre.

In Idaho, local government property assessors calculate an applicant's level of eligible property via an automated data system based on their qualifying income. However, in addition, the Idaho Tax Commission, the state's taxing authority, ensures local government only applies relief to eligible properties by requiring two annual reports from local government which are used to verify that taxpayers are only receiving relief on eligible property based on their qualifying income.

RECOMMENDATION #3

We recommend the department:

- A. *Develop and implement a quality control process to improve department efforts to ensure taxpayers applying for the Property Tax Assistance Program or the Disabled American Veteran's Exemption only receive property tax relief on eligible land and improvements, and*
 - B. *Investigate ways to automate the calculation process within Orion to ensure taxpayers are receiving relief on eligible land and improvements.*
-

Some Taxpayers Are Not Receiving Benefits Based on Qualifying Income

As discussed previously in this report, qualified taxpayers for PTAP and DAV receive a percentage of relief on their property taxes based on a series of income tiers. The taxable market value of a qualified taxpayer's property is taxed at a rate determined by the legislature and then subsequently multiplied by percentage based on the income from the preceding calendar year. As part of the relief determination process, department staff enter the amount of the qualifying income in Orion and manually select the appropriate tax class code which corresponds to the reduction for which the taxpayer is eligible based on their income. If a reviewing staff member selects the incorrect tax class code, an applicant will either overpay or underpay on their property taxes. As part of the 17,035 granted PTAP applicants and 2,015 granted DAV applicants we reviewed for 2013, we also compared the qualifying income with the tax rate class code selected by department staff as part of the review process to determine if an applicant's qualifying income corresponded with the correct tax rate class code. As part of this analysis, we did not question the accuracy of the amount of the qualifying income entered into Orion. Our work identified 324 PTAP and 15 DAV applicants who did not receive the appropriate tax rate reduction based on their qualifying income. Table 8 on page 21 summarizes the benefit errors we identified as a result of the department selecting the incorrect tax class code based on an applicant's qualifying income, including overpayments and underpayments of property taxes paid to local government.

Table 8
**2013 Underpayment and Overpayment Errors Identified
 Due to Incorrect Tax Class Code Assignment**

Program	Minimum Underpayment	Maximum Underpayment	Average Underpayment	Total Underpayment
The Property Tax Assistance Program	\$8.77	\$878.71	\$232.21	\$42,958.99
The Disabled American Veterans Exemption	\$15.59	\$616.86	\$262.35	\$2,098.83
Program	Minimum Overpayment	Maximum Overpayment	Average Overpayment	Total Overpayment
The Property Tax Assistance Program	\$16.03	\$999.01	\$351.99	\$48,574.47
The Disabled American Veterans Exemption	\$215.06	\$954.62	\$430.46	\$3,013.20

Source: Compiled by the Legislative Audit Division from department records.

The Department Does Not Consistently Ensure Relief Aligns With Income

According to department staff, since property records carry forward from year-to-year in Orion, staff who review applications may forget to update records with new information, including the correct qualifying income and the appropriate tax rate class code for the current year. According to staff, while the department has developed procedures for reviewing supporting income documentation, there currently is not a quality control process in place to ensure that the income determinations made by field staff are accurate in Orion. During the course of our audit work, the department indicated there may be solutions to automate the assignment of the correct tax class code within Orion with an income range, as automation of this function would be the best solution to resolve human errors. They also acknowledged the need to establish a quality control process to check the accuracy of income determinations based on the qualifying income of taxpayers applying for relief. During the audit, department staff indicated they were in the process of developing management tools to verify the accuracy of income data entered by field staff.

RECOMMENDATION #4

We recommend the department:

- A. *Develop and implement a quality control process to improve department efforts to ensure taxpayers applying for the Property Tax Assistance Program or the Disabled American Veteran's Exemption receive property tax relief based on their qualifying income, and*
 - B. *Investigate ways to automate the assignment of tax class codes within Orion to ensure taxpayers are receiving relief based on their qualifying income.*
-

Chapter IV – Property Tax Relief Distribution

Introduction

In Montana, there are four programs administered by the Department of Revenue (department) which provide property tax relief to individual taxpayers, including the Property Tax Assistance Program (PTAP), the Extended Property Tax Assistance Program (EPTAP), the Disabled American Veterans (DAV) Exemption, and the Elderly Home Owner/Renter Credit (elderly credit). PTAP, EPTAP, and DAV reduce taxes through a reduction in the taxable value on eligible property and are administered by the department's Property Assessment Division (PAD). The elderly credit program provides an income tax credit based on property taxes or rent paid and is administered by the department's Business and Income Tax Division (BITD). As part of our third objective, we examined how usage for the elderly credit program was distributed across the state in 2012. We also examined if there are taxpayers leveraging multiple property tax relief programs and how rates of participation compare with socioeconomic data for program applicants. We determined that while there is no prohibition for taxpayers to participate in multiple programs, there is limited coordination between the various relief programs administered by the department. We also determined the department could examine their outreach efforts to assess the distribution of property tax relief benefits statewide. This chapter discusses these issues further.

The Elderly Home Owner/Renter Credit Program

As discussed in the background chapter of this report, taxpayers who are 62 years or older and have a gross household income of less than \$45,000 may be eligible for this credit. This program is available for both homeowners and renters and provides relief based on property tax billed or rent-equivalent paid. While property tax relief available through PTAP, EPTAP, and DAV most directly impacts the operational revenue of local government as a result of a reduction in the tax rate applied to a property's taxable market value, the elderly credit is administered as an income tax credit and results in a reduction to the state's general fund. As part of our audit work, we examined the usage of the elderly credit to assess how the program is distributed geographically across Montana for participants. Figure 1 on page 26 illustrates the percentage of participants in the elderly credit relative to the total number of individuals aged 62 and older in each of Montana's 56 counties, as identified by the American Community Survey, an ongoing statistical survey by the U.S. Census Bureau. As illustrated by Figure 1 on page 24, we noted that participation in the elderly credit generally skewed greater in the western and central portions of the state, including more populous areas such as Yellowstone County in the eastern portion of the state.

on the radio, and outreach with veteran and senior support groups and agencies. The department actively encourages taxpayers to apply for multiple programs and obtain the maximum amount of benefits possible. As part of our audit work, we obtained information from the department on the number of participants from 2012 in each of the four programs administered by the department to assess the extent to which individual taxpayers are leveraging multiple property tax relief programs. According to data obtained from the department, in 2012, there were a total of 37,730 individuals who received benefits from the four programs. Table 9 represents the number of granted participants in each program for 2012.

Table 9
**Number of Property Tax Relief Program
 Granted Participants for 2012**

Property Tax Relief Program Name	Number of Participants
The Elderly Home Owner/Renter Credit	20,324
The Property Tax Assistance Program	13,054
The Extended Property Tax Assistance Program	2,389
The Disabled American Veterans Exemption	1,963

Source: Compiled by the Legislative Audit Division from department records.

Due to the fact that the EPTAP, PTAP, and DAV are administered by the PAD and the elderly credit is administered by BITD, there was not a common identifier available between the four programs to easily determine the number of individuals who are obtaining property tax relief from multiple programs. While the PAD does collect social security numbers on EPTAP, PTAP, and DAV applications, department staff do not routinely use that information or enter it into Orion. Conversely, BITD collects social security numbers as part of its application process for taxpayers for the elderly credit. Consequently, we were able to obtain social security numbers for approximately 55 percent of all granted applications for EPTAP, PTAP, and DAV combined. We had social security numbers for 100 percent of the elderly credit granted participants. Based on available social security numbers, we were then able to match approximately 13 percent of the combined EPTAP, PTAP, and DAV participants with elderly credit participants from 2012. This number represents taxpayers we were able to identify who leveraged benefits from multiple property tax relief programs for 2012. In order to estimate how many individuals leveraged the elderly credit in concert with one or more program administered by PAD, we estimated the number of individuals by the percentage of available social security numbers available. For example, based on social security matches, we identified 924 PTAP applicants who also leveraged the elderly credit. We estimated that these 924 individuals only represented 55 percent of potential PTAP granted applicants who also received a benefit from the elderly credit. We were able to determine the number of individuals who obtained relief from multiple PAD

programs based on names and addresses. The following table represents the number of granted applicants from the four programs administered by the department who leveraged property tax relief from multiple programs for 2012.

Table 10
**2012 Number of Individuals Who Accessed Property Tax Relief
From Multiple Programs**

Population Definition	Elderly Credit	PTAP	EPTAP	DAV	Total Program Applicants
2012 total granted applicants	20,324	13,054	2,389	1,963	37,730
2012 granted applicants who accessed the elderly credit in concert with one or more PAD programs*	2,204	1,680	511	13	4,408
2012 granted applicants who accessed multiple PAD programs only	NA	322	323	21	666

Source: Compiled by the Legislative Audit Division from department records.

*Represents estimated number based on percentage of social security matches.

Should Property Tax Relief Programs be More Closely Coordinated?

As discussed, there is no prohibition against a taxpayer receiving property tax relief with multiple programs. However, a taxpayer may not receive relief in excess of their property tax liability. As part of our work, we noted individuals who had received a 100 percent reduction in their property taxes through DAV, but also received a refund through the elderly tax credit for 2012. When we discussed this with department staff, they indicated that there may be circumstances where this scenario could occur. Department staff reported property tax relief administered by PAD only results in a reduction of statewide assessed taxes and not on any local assessments, such as waste disposal fees levied by local government. As a result, a taxpayer could receive a 100 percent reduction through DAV, but still obtain a refund through the elderly credit for locally determined assessments. Department staff indicated that as part of the elderly credit taxpayers must provide a copy of their prior year's property tax bill or rent equivalent paid, which would prevent the application of a credit in excess of property taxes paid. However, it is conceivable that taxpayers new to the relief programs could obtain relief in excess of their liability in their first year, due to the fact that relief is based on last year's property taxes. However, the department does not compare usage of the programs between taxpayers. According to department staff, there is little coordination between relief programs administered by PAD and BITD.

While there is no prohibition against taxpayers leveraging relief through multiple programs, there appears to be potential for a taxpayer to obtain relief in excess of their tax liability. This risk warrants the department to consider more closely coordinating relief provided by the four programs administered by the department. In addition, each of the four property tax relief programs administered by the department target unique constituents, with disparate and often fragmented eligibility requirements. For example, the four programs each have their own set of income thresholds, with different income definitions and supporting documentation requirements. There are also differences in eligible property thresholds between the programs, including limits on taxable market value and the number of acres eligible for relief. These various differences create confusion for individual taxpayers and increase the administrative burden on the department to ensure that relief is only obtained by eligible taxpayers.

CONCLUSION

Property tax relief efforts in Montana are generally fragmented and uncoordinated, with disparate and often confusing eligibility requirements making it challenging for individual taxpayers to interpret and the department to administer.

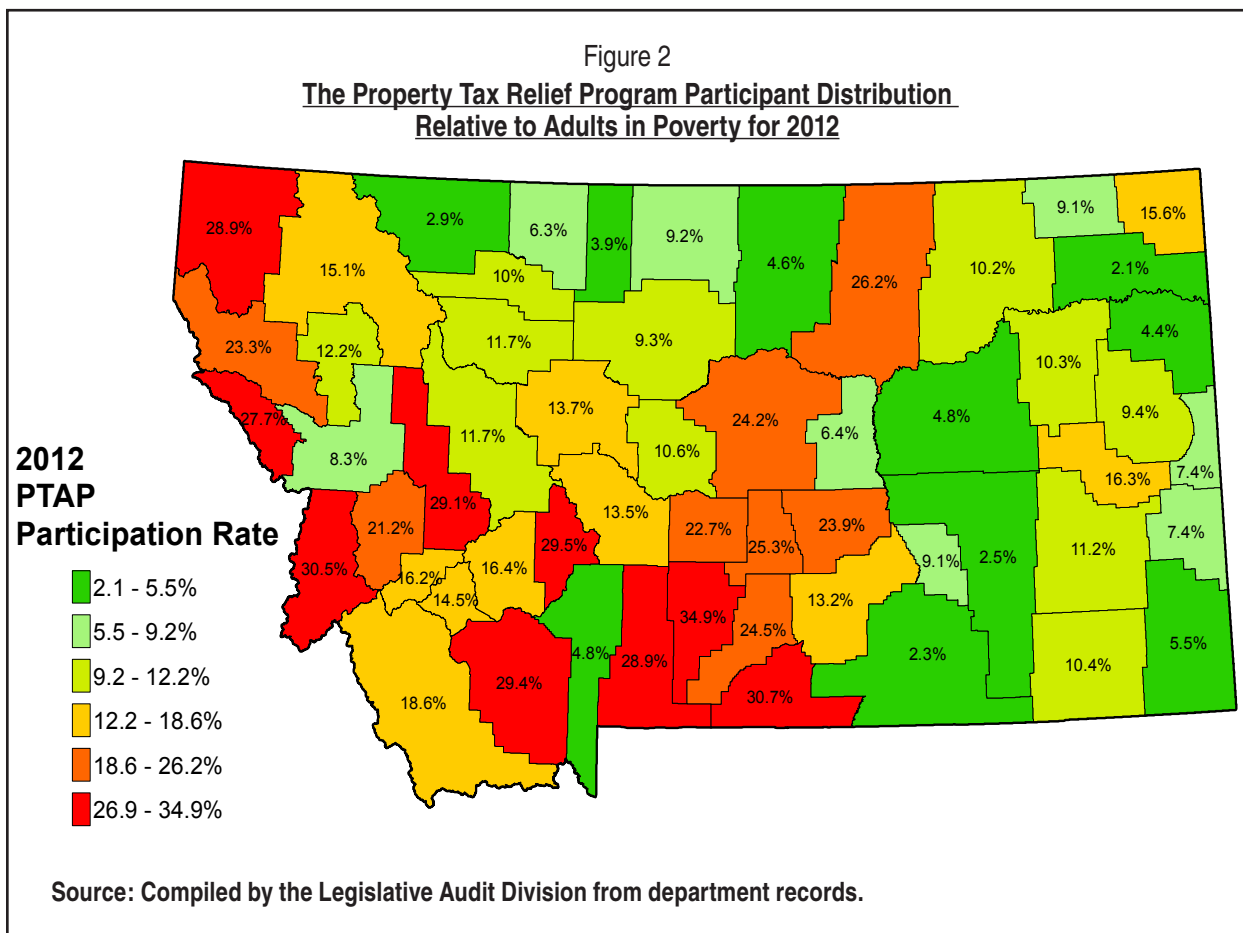
Property Relief Program Distribution

In order to get a better sense of the geographic distribution of each program, based on program data from 2012 obtained from the department, we plotted the usage for each program by county across Montana. As part of our analysis, we noted the general trend of geographic participation in property tax relief programs administered by the department was greater in the western portion of the state. We noted there were several counties in central and eastern Montana with no EPTAP applicants; however, this is attributable to the fact that EPTAP is available by invitation only for taxpayers who experienced significant increases in their property values during the most recent reappraisal cycle. For DAV, we noted there were six counties in eastern Montana for which there were no DAV participants in 2012, which is likely attributable to a lack of 100 percent disabled veterans in those counties or potential applicants not applying for the programs.

How Is Property Tax Relief Distributed in Montana?

As part of our audit work, we also examined how property tax relief program usage is distributed statewide relative to population groups targeted by a specific program. For DAV and PTAP, we obtained information on low-income and veterans' disabled populations from the American Community Survey. We did this in order to assess

program participation relative to the potential number of program participants in a certain population group. For PTAP, we obtained census information on the number of adults 18 years and older as defined by the federal government as living in poverty. For DAV, we obtained information on veterans considered greater than 70 percent disabled, as data for veterans currently rated 100 percent disabled was unavailable. For DAV, participation relative to disability status was generally higher in more populous counties in the western portion of the state as expected. However, rates of participation for PTAP varied widely for individuals in poverty. Rates of participation in PTAP relative to adults in poverty ranged from 2.1 to 34.9 percent. Figure 2 plots the distribution of property tax relief in the state in relation to adults in poverty for the 13,054 granted PTAP applicants for 2012.



As illustrated in Figure 2, there again appears to be a general trend of greater participation in the western and central portion of the state. However, the disparity in rates of participation generates questions as to why participation in some counties is only two percent and in others nearly 35 percent. Some possible explanations include factors such as large transient populations of students in some counties or low rates of homeownership in some counties. Department staff stressed that ultimately

it is the responsibility of individual taxpayers to apply for the relief programs. They speculated that there may be a number of factors contributing to the disparity of rates of participation, including areas of the state with high unemployment affected more acutely by the recent recession, low-rates of home ownership in some areas, or a self-sufficient attitude on the part of some taxpayers and an accompanying reluctance to apply for government benefits. The department indicated there may be a number of variables which could be considered when examining rates of participation in property tax relief. However, while they actively advertise the various property tax relief programs in a number of ways, they have not routinely analyzed the distribution of relief to gauge either their outreach efforts or participation rates.

The Department Should Assess Outreach Efforts and Benefit Distribution

Section 15-9-101, MCA, outlines the department's role to adjust and equalize the valuation of taxable property to do all things necessary to secure a fair, just, and equitable valuation of all taxable property among counties, between the different classes of property, and between individual taxpayers. Through its property tax function, the department is responsible for administering Montana's property tax laws, including the valuation and assessment of real and personal property throughout the state for property tax purposes. The PAD is responsible for ensuring that all classes of property in the state are valued uniformly and equally throughout the state. The work of the division is critical to the operation of local government, since its valuations are used to fund services provided by local government, including public schools, law enforcement, fire protection, road and bridge construction and maintenance, transportation, and other public assistance.

As discussed earlier, many states—including Montana—have implemented various property tax relief measures to alleviate the property tax burden. The guiding notion behind property tax relief is to provide assistance to those individuals whom the current valuation process may disproportionately impact. Audit work indicated that impact of property tax relief for PTAP and DAV ranged from .02 percent to 2.82 percent of total property taxes levied in each county. In addition, as discussed in the previous section, there are taxpayers obtaining relief from multiple programs in the state, which may be of interest to the department as it administers these various relief programs. The uncertainty of which variables are impacting participation highlights the need for the department to actively analyze their outreach efforts and use that information to aid in the administration of property tax relief programs. The department's Tax Policy Research function routinely analyzes economic data and tax compliance information which affect department operations and would likely be a resource to examine the distribution of property tax relief in the state.

RECOMMENDATION #5

We recommend the department actively examine their outreach efforts to assess benefit distribution and aid in the administration of property tax relief programs.

**2013 Property Tax Assistance Program and Disabled
American Veterans Exemption Benefit Distribution**

County	DAV Total Participants	DAV Total Benefits	DAV Average Benefit	PTAP Total Participants	PTAP Total Benefits	PTAP Average Benefit
Beaverhead	11	\$ 14,859.90	\$1,350.90	222	\$ 114,658.95	\$ 516.48
Big Horn	9	5,548.28	616.48	75	27,349.45	364.66
Blaine	8	5,724.45	715.56	49	16,593.01	338.63
Broadwater	22	21,431.96	974.18	132	58,988.93	446.89
Carbon	27	34,818.57	1,289.58	243	121,980.26	501.98
Carter	3	1,440.86	480.29	13	2,118.19	162.94
Cascade	271	334,505.73	1,234.34	1,498	889,344.90	593.69
Chouteau	11	8,201.40	745.58	64	21,115.80	329.93
Custer	26	24,304.80	934.80	198	101,135.44	510.79
Daniels	2	804.56	402.28	18	3,172.08	176.23
Dawson	6	6,098.58	1,016.43	90	39,809.88	442.33
Deer Lodge	20	21,388.78	1,069.44	383	191,275.15	499.41
Fallon	0	0.00	0.00	18	2,015.82	111.99
Fergus	33	32,840.33	995.16	330	161,804.73	490.32
Flathead	175	287,288.74	1,641.65	1,532	1,067,572.95	696.85
Gallatin	99	175,147.84	1,769.17	582	418,966.36	719.87
Garfield	0	0.00	0.00	3	985.12	328.37
Glacier	6	4,917.45	819.57	82	32,380.14	394.88
Golden Valley	4	1,949.09	487.27	25	6,401.67	256.07
Granite	5	5,699.11	1,139.82	83	40,618.59	489.38
Hill	20	23,646.97	1,182.35	232	117,906.03	508.22
Jefferson	43	43,387.44	1,009.01	177	96,404.10	544.66
Judith Basin	6	1,200.50	200.08	24	5,002.22	208.43
Lake	45	61,537.94	1,367.51	643	362,661.78	564.02
Lewis & Clark	169	242,377.39	1,434.19	731	474,535.53	649.16
Liberty	3	1,244.30	414.77	17	4,901.86	288.34
Lincoln	114	103,021.92	903.70	1,040	488,921.12	470.12
Madison	16	13,366.26	835.39	190	100,655.97	529.77
McCone	1	162.03	162.03	18	4,467.85	248.21
Meagher	4	1,284.97	321.24	38	14,194.16	373.53
Mineral	23	28,684.30	1,247.14	189	114,513.77	605.89
Missoula	156	294,149.36	1,885.57	1,612	1,381,604.42	857.07
Musselshell	29	15,472.91	533.55	124	36,895.38	297.54
Park	27	33,609.95	1,244.81	452	294,438.08	651.41
Petroleum	1	602.61	602.61	8	1,819.06	227.38
Phillips	1	297.31	297.31	124	39,130.28	315.57
Pondera	11	7,435.31	675.94	117	39,320.67	336.07
Powder River	0	0.00	0.00	22	4,923.94	223.82
Powell	14	9,397.50	671.25	201	92,761.31	461.50

County	DAV Total Participants	DAV Total Benefits	DAV Average Benefit	PTAP Total Participants	PTAP Total Benefits	PTAP Average Benefit
Prairie	3	\$ 887.09	\$ 295.70	39	\$ 6,598.31	\$ 169.19
Ravalli	173	220,029.86	1,271.85	1,455	855,878.97	588.23
Richland	0	0.00	0.00	49	14,112.27	288.01
Roosevelt	6	2,509.21	418.20	44	13,758.47	312.69
Rosebud	11	4,674.66	424.97	57	11,245.24	197.28
Sanders	81	74,788.17	923.31	524	240,665.15	459.28
Sheridan	0	0.00	0.00	42	10,334.22	246.05
Silver Bow	62	66,694.81	1,075.72	821	428,738.89	522.22
Stillwater	21	25,027.99	1,191.81	177	84,024.81	474.72
Sweet Grass	6	7,045.10	1,174.18	105	62,121.17	591.63
Teton	20	13,092.30	654.61	108	40,699.48	376.85
Toole	7	2,918.54	416.93	49	15,938.69	325.28
Treasure	0	0.00	0.00	5	1,049.53	209.91
Valley	7	6,223.29	889.04	88	26,643.41	302.77
Wheatland	7	2,815.29	402.18	45	10,924.37	242.76
Wibaux	0	0.00	0.00	7	1,418.14	202.59
Yellowstone	223	307,100.97	1,377.13	2,089	1,441,413.31	690.00
Total	2,048	\$2,601,656.65	\$ 771.19	17,303	\$10,258,909.37	\$409.50

In order to calculate the total benefit, additional information was included in this analysis which may have resulted in a nonsignificant overstatement of the number of participants and amount of total benefits.

2012 Elderly Home Owner/ Renter Credit Distribution

County	Granted Participants	Total Credit	Average Credit
Beaverhead	193	\$ 80,485.00	\$417.02
Big Horn	83	32,357.00	\$389.84
Blaine	89	35,620.00	\$400.22
Broadwater	107	47,069.00	\$439.90
Carbon	168	70,102.00	\$417.27
Carter	5	2,027.00	\$405.40
Cascade	1,838	811,360.00	\$441.44
Chouteau	57	21,979.00	\$385.60
Custer	217	87,240.00	\$402.03
Daniels	13	4,323.00	\$332.54
Dawson	111	39,573.00	\$356.51
Deer Lodge	223	93,703.00	\$420.19
Fallon	17	7,314.00	\$430.24
Fergus	199	86,603.00	\$435.19
Flathead	2,302	1,192,138.00	\$517.87
Gallatin	1,323	736,130.00	\$556.41
Garfield	7	2,675.00	\$382.14
Glacier	69	24,804.00	\$359.48
Golden Valley	7	2,049.00	\$292.71
Granite	44	17,931.00	\$407.52
Hill	255	112,121.00	\$439.69
Jefferson	188	82,387.00	\$438.23
Judith Basin	15	5,544.00	\$369.60
Lake	696	365,417.00	\$525.02
Lewis & Clark	1,453	716,761.00	\$493.30
Liberty	19	6,031.00	\$317.42
Lincoln	353	151,195.00	\$428.31
Madison	155	62,568.00	\$403.66
McCone	11	2,793.00	\$253.91

County	Granted Participants	Total Credit	Average Credit
Meagher	30	\$ 12,378.00	\$ 412.60
Mineral	111	48,154.00	433.82
Missoula	2,633	1,392,729.00	528.95
Musselshell	70	25,383.00	362.61
Park	482	223,691.00	464.09
Petroleum	3	252.00	84.00
Phillips	72	31,222.00	433.64
Pondera	76	27,530.00	362.24
Powder River	5	2,142.00	428.40
Powell	120	46,289.00	385.74
Prairie	13	6,011.00	462.38
Ravalli	946	417,503.00	441.34
Richland	90	33,976.00	377.51
Roosevelt	52	15,501.00	298.10
Rosebud	40	14,961.00	374.03
Sanders	274	121,895.00	444.87
Sheridan	43	15,766.00	366.65
Silver Bow	888	373,331.00	420.42
Stillwater	134	53,697.00	400.72
Sweet Grass	67	31,300.00	467.16
Teton	114	40,938.00	359.11
Toole	57	18,159.00	318.58
Treasure	5	1,494.00	298.80
Valley	122	47,838.00	392.11
Wheatland	28	9,303.00	332.25
Wibaux	2	899.00	449.50
Yellowstone	3,474	1,642,212.00	472.72
Out-of-State	156	86,692.00	555.72
Total	20,324	\$9,641,545.00	\$403.28

DEPARTMENT OF REVENUE

DEPARTMENT RESPONSE



Mike Kadas
Director

Montana Department of Revenue



Steve Bullock
Governor

A-1

August 11, 2014

Tori Hunthausen, Legislative Auditor
Legislative Audit Division
Room 160, State Capitol
P.O. Box 201705
Helena, MT 59620-1705

RECEIVED
AUG 13 2014
LEGISLATIVE AUDIT DIV.

Dear Ms. Hunthausen:

Thank you for the opportunity to respond to the performance audit on Property Tax Relief. Our responses to the current status of those recommendations are as follows:

Audit Recommendation #1: Concur.

We recommend the Department of Revenue develop and implement additional management tools to improve how they verify the occupancy requirements of Property Tax Assistance Program.

The audit found 23, or 0.1% of the 17,035 granted PTAP applications in error and 26, or 1.2% of the 2,015 DAV applications in error. This resulted in a benefit error of \$48,000 of the \$12,860,566 in total benefits, or 0.4% rate of benefit error. Conclusively verifying occupancy, beyond the applicant's signature of affirmation, is extremely difficult given privacy concerns and resource limitations. The department will not deny an application, even though the occupancy is suspect, without documentation. Documentation is difficult to obtain without visiting each residence and physically checking an applicant's occupancy on a monthly basis.

The department has implemented tools that generate reports to identify PTAP and DAV records that have had a change in ownership. This allows the comparison between the current and previous owner names to determine whether an actual change in ownership occurred. However, it is important to note that ownership is not necessarily evidence of occupancy. The reports also provide the transfer date which allows staff to determine

whether an applicant owned the property for at least 7 months of the prior year, as required by law.

The department recommends legislative changes to the occupancy requirement, such as, acceptance of an applicant's affirmation, removal of the occupancy requirement, or include clear criteria in identifying occupancy.

Audit Recommendation #2: Concur.

We recommend the Department of Revenue:

- 1. Develop and implement additional management tools to improve income verification between the Property Assessment Division and the Business and Income Tax Division for the Property Tax Assistance Program and the Disabled American Veteran's Exemption, and*
- 2. Investigate ways to simplify income documentation provided by applicants for property tax relief programs administered by the department, including the Property Tax Assistance Program and the Disabled American Veteran's Exemption.*

The auditors conducted a comparison of income in the *Orion* and *GenTax* systems for approximately half of the PTAP and DAV granted applications. They found 223, or 2.4% of the approximately 9,000 PTAP applications reviewed in error and 13, or 1.3% of the approximately 1,000 DAV applications reviewed in error. This resulted in a benefit error of over \$23,000 of the \$12,860,566 in total benefits, or 0.2% rate of benefit error.

The current verification process begins with the PAD field staff verifying income upon receipt of an application and appropriate documentation. When the income information is questionable the field staff forwards the application to the central office for further review. The central office reviews the income documentation and, if needed, consults with BIT to help determine whether the applicant's income meets the requirements for the program.

The department recognizes that some errors have occurred in verifying the income of taxpayers. In an effort to decrease the number of errors, the department implemented tools that generate quality assurance reports to allow for multiple social security numbers on a single property record to enable income verification of multiple owner/applicants. Additional quality assurance reports are generated to ensure that social security numbers and income information are entered onto all program applicants' *Orion* records. Having this data in both the *Orion* and *GenTax* systems enables the department to compare the income reported on the property tax program's application to the applicant's income tax return. This is a step toward automating the process of verifying the applicant's income. Non-income tax filers will still be an income

verification challenge due to the lack of an income tax return. However, this concern is somewhat mitigated because many of the applicants are elderly with income that does not significantly change from year to year. Additional quality assurance reports identifying income changes over a given threshold will also be developed, which will “flag” records to review.

Given these difficulties under current law, the department recommends legislation to simplify the income eligibility requirements by defining “income” consistently between each program. Further, that definition of income should be kept simple to minimize taxpayer confusion and optimize administrative efficiency. Additionally, the social security number match between the property and income tax systems lends itself to changing the processing of the applications to an electronic format. This is a project that the department plans to implement in the future.

Audit Recommendation #3: Concur.

We recommend the Department of Revenue:

1. *Develop and implement a quality control process to improve department efforts to ensure taxpayers applying for the Property Tax Assistance Program or the Disabled American Veteran’s Exemption only receive property tax relief on eligible land and improvements, and*
2. *Investigate ways to automate the calculation process within Orion to ensure taxpayers are receiving relief on eligible land and improvements.*

The audit found 525, or 3.0% of the 17,035 granted PTAP applications in error for taxpayers receiving in excess of the \$100,000 taxable market value of their property. A majority of the errors found or 363 of the 525, are due to software system rounding in *Orion* of \$1-\$2 over the \$100,000 limit in taxable market value. The department will implement quality assurance reports to identify applicants who receive the benefit on more than the \$100,000 taxable market value. Those records will be reviewed to ensure that the amount over the limit is due to IT software system rounding only.

The audit also found 201, or 1.2% of the 17,035 PTAP applications in error and 27, or 1.3% of the 2,015 DAV applications in error, for taxpayers receiving the benefit on more than 5 acres of land resulting in nearly \$19,000 of the \$12,860,566 in total benefits, or 0.1% rate of benefit error. The program benefit is limited to 5 acres of land. Many of these errors are attributable to incorrect data entry in *Orion*, but did not result in the applicants receiving more of a benefit than they were entitled. This is a data entry training issue which the department will address.

The department has implemented tools that generate quality assurance reports that identify PTAP and DAV granted records where the benefit was applied to land in excess

of five acres for review. Additionally, the department will implement a process for mass mailing the decision letters, to ensure that staff completes the quality assurance for both the rounding errors and excess land errors before decision letters are mailed to the applicants.

The department will look into the feasibility of automating the process to reduce human error.

Audit Recommendation #4: Concur.

We recommend the Department of Revenue:

- 1. Develop and implement a quality control process to improve department efforts to ensure taxpayers applying for the Property Tax Assistance Program or the Disabled American Veteran's Exemption receive property tax relief based on their qualifying income; and*
- 2. Investigate ways to automate the assignment of tax class codes within Orion to ensure taxpayers are receiving relief based on their qualifying income.*

The department has implemented tools that generate quality assurance reports that identify income to be "flagged" for eligibility review and verification. The department also has implemented quality assurance reports identifying class code errors to review and correct, prior to the certification of values. This report identifies PTAP and DAV applications that have a mismatch in the class codes and tax rates. The results are compared to the correct code, which is based upon the exemption income information. The reports are included in our annual work for processing PTAP and DAV applications.

Automation of the income information between the *Orion* and *GenTax* systems is more feasible with a simple and consistent definition between programs, which would require legislative action to amend current law. In the meantime, the department will look into the feasibility of automation.

Audit Recommendation #5. Concur.

We recommend the Department of Revenue actively examine their outreach efforts to assess benefit distribution and aid in the administration of property tax relief programs.

The PTAP and DAV assistance programs are benefits granted to eligible property taxpayers. It is the taxpayer's responsibility to apply and provide the documentation for

qualification. The property taxes for qualified applicants are calculated using a reduced tax rate.

The department seeks to maximize the participation in the programs in a number of ways, such as: local advertisements, public radio announcements, the department website, providing information in each of our county field offices as well as an insert in the Montana income tax booklets. Additionally, the department has mailed post cards to potential applicants for the past two years. As a result of these outreach efforts, the department noted an increase of applications received and applications granted of approximately 20% between 2012 and 2013. It is through these efforts that the department is working to inform the public about the tax assistance programs. The department intends to amend the program forms to include a check box for the applicant to tell us how he/she heard about the program, to gauge and then improve the effectiveness of our outreach efforts.

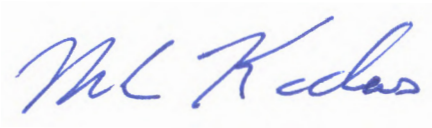
The audit compared the federal guidelines for poverty to the number of granted applications in each county in an effort to assess distribution. The use of the federal poverty guidelines to gauge PTAP distribution makes the assumption that the federal income eligibility requirements are the same as the income requirements for the PTAP program, which they are not. The federal poverty guidelines are based upon family size. A family may be classified, according to the federal guidelines, as living in poverty; but the income of the applicant may exceed the Montana statutory program guidelines, which would disqualify them from the PTAP program.

The use of the federal poverty guidelines also assumes that those individuals that are living in poverty are homeowners. The department's statewide analysis by county considers poverty level, population, home ownership and median household income. All factors are important in determining distribution. The poverty level alone is of little relevance. The department's analysis shows that as income levels increase, in a given portion of a county, the PTAP applications decrease and when income levels decrease the corresponding PTAP applications increase. In addition, the distribution of PTAP applications corresponds to the number of owner occupied homes. As home ownership increases, so does the number of PTAP applications and as home ownership decreases, the number of PTAP applications decreases. In other words, the utilization of the programs seems to fall in line with the state eligibility requirements for income and owner occupied homes rather than only the federal guidelines for poverty.

Additionally, the department currently publishes in its Biennial Report the property tax impacts, i.e., number of participants, loss in state revenue, tax shifts, total tax benefits, and the average tax benefit, of the PTAP, DAV, EPTAP, and the Elderly Homeowner/renter Credit. The department will continue to enhance these analysis efforts.

Again, thank you for allowing the department the opportunity to review and respond to the audit report and your recommendations.

Sincerely,

A handwritten signature in blue ink that reads "Mike Kadas". The signature is written in a cursive style with a large, stylized "M" and "K".

Mike Kadas
Director