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DEC 15 2011

December 13, 2011

FILE # ML-46905-11  
I.D. # 46905

**OPINION COMMITTEE**

The Honorable Greg Abbott  
Attorney General of Texas  
P.O. Box 12548  
Austin, Texas 78711-2548

**RQ-1029-GA**

Dear General Abbott:

I ask for your opinion regarding the following question:

In determining the market value of a residence homestead for ad valorem tax purposes, is the chief appraiser of an appraisal district required to take into consideration the value of other residential property that was sold at a foreclosure sale conducted in any of the three years preceding the tax year in which the residence homestead is being appraised and meets the other requirements of Section 23.01(c)(1), Tax Code, or may the chief appraiser exclude the property from consideration if the chief appraiser determines, based on the price for which the property sold at the foreclosure sale or other factors, that the foreclosure sale was not a sale for market value?

Section 1(b), Article VIII, Texas Constitution, requires generally that real and tangible personal property be taxed in proportion to its "value, which shall be ascertained as may be provided by law." The courts have construed "value" for purposes of Section 1(b) as meaning "reasonable cash market value." *Travis Central Appraisal District v. FM Properties Operating Company*, 947 S.W.2d 724, 732 (Tex. App.--Austin 1997, writ denied).

Section 23.01(a), Tax Code, generally requires that all taxable property be appraised at its "market value." Section 23.01(b), Tax Code, requires that the market value of property be determined by the application of "generally accepted appraisal methods and techniques." Section 23.0101, Tax Code, requires the chief appraiser, in determining the market value of property, to consider the cost, income, and market data comparison methods of appraisal and use the most appropriate method. Section 23.013, Tax Code, specifies the procedure to be followed in using the market data comparison method of appraisal. Section 1.04(7), Tax Code, defines "market value" to mean the price for which a property would transfer for cash or its equivalent under prevailing market conditions if certain requirements are met, including the requirement of Paragraph (C) of that subdivision that "both the seller and purchaser seek to maximize their gains and neither is in a position to take advantage of the exigencies of the other."



Section 5 of the Summary of the International Association of Assessing Officers Standard on Sales Verification prepared by the comptroller's property tax assistance division provides that sales should be verified to determine whether they reflect the market value of real property and that sales should be excluded if they fail to meet the criteria for an arm's length transaction. Section 5.3 lists sales that are generally invalid but may be used if carefully verified. Among the sales generally considered invalid are sales involving government agencies, sales involving financial institutions as buyer or seller, and forced sales resulting from a judicial order. Section 5.13 also provides that short sales, "as with foreclosures," should not be used.

Chapter 619 (H.B. 1038), Acts of the 81st Legislature, Regular Session, 2009, amended Section 23.01, Tax Code, by adding Subsection (c). That subsection provides in part:

Notwithstanding Section 1.04(7)(C), in determining the market value of a residence homestead, the chief appraiser may not exclude from consideration the value of other residential property that is in the same neighborhood as the residence homestead being appraised and would otherwise be considered in appraising the residence homestead because the other residential property . . . was sold at a foreclosure sale conducted in any of the three years preceding the tax year in which the residence homestead is being appraised and was comparable at the time of sale based on relevant characteristics with other residence homesteads in the same neighborhood.

(The bill also prohibits excluding from consideration the value of residential property that has a market value that has declined because of a declining economy, but that provision is not the subject of this request.) Representative Paxton, the author of the bill, testified at the House Ways and Means Committee's hearing on the bill on March 11, 2009, that the bill was intended to require appraisal districts to include foreclosed properties in their appraisals. He related a personal experience in which an appraisal district excluded foreclosed properties in valuing his home, thereby artificially inflating the value of the home, and argued that as a matter of fairness appraisal districts should consider all sales, whether for high or low prices.

The introduced version of the bill did not include the cross-reference to Section 1.04(7)(C), Tax Code. Jim Robinson, the chief appraiser of the Harris County Appraisal District, testified on behalf of the Texas Association of Appraisal Districts at the House Ways and Means Committee's hearing on the bill on March 11, 2009, that Section 1.04, Tax Code, generally precludes chief appraisers from considering foreclosure sales in appraising property, although the Harris County Appraisal District does consider them in appraising property if they are the predominant type of sale in the area. He suggested that it might be preferable to add language to address the conflict between Section 1.04 and proposed Section 23.01(c). Similarly, Cheryl Johnson testified on behalf of Galveston County Taxpayers that foreclosure sales do not generally represent arm's length transactions and that it would be necessary to amend the Tax Code if the intent were to consider those sales in spite of the requirements of Section 1.04. Representative Oliveira, the chair of the committee, said the bill could be taken up by the

committee the following week if the bill were amended to address the conflict with Section 1.04.

The reference to Section 1.04, Tax Code, was added by the house committee substitute for the bill. At the hearing on March 18, 2009, at which the committee adopted the committee substitute, Representative Paxton testified that the bill requires sales of distressed properties to be considered in valuing property. Representative Oliveira also testified that appraisal districts should be required to consider sales of distressed properties in valuing property. They acknowledged that the committee substitute addressed the issue of the conflict with the Tax Code's definition of "market value" raised at the prior committee hearing. When the bill was considered on the house floor on March 30 and 31, 2009, Representative Paxton testified that the bill was intended to prohibit appraisal districts from excluding distressed and foreclosed properties from consideration in valuing property.

At the hearing of the Senate Committee on Finance on May 23, 2009, Senator Eltife testified that the purpose of the bill was to prevent appraisal districts from overlooking relevant foreclosed or distressed properties in appraising property with the goal of having residential appraisals reflect the true market value of property. Senator Patrick, the sponsor of the bill, likewise testified on the Senate floor on May 26, 2009, that the bill was intended to prevent appraisal districts from overlooking properties that have been foreclosed on during the past three years or have distressed values due to a declining economy.

The House Research Organization's analysis of the bill states that appraisers have generally understood the willful and arm's length transaction requirement in Section 1.04(7)(C), Tax Code, to preclude inclusion of recently foreclosed properties but that the bill would amend the Tax Code to require an appraisal district to include comparable foreclosed and distressed homes when valuing a residence homestead. The bill would direct appraisers, when valuing a homestead, to consider the value of properties that were foreclosed on during the prior three years and were comparable to the homestead at the time of the foreclosure sale. The analysis noted that the house committee substitute differed from the introduced version of the bill by directing appraisers to consider foreclosed properties and distressed properties regardless of the requirement in Section 1.04(7)(C) that sales be willful and at arm's length.

The comptroller has posted answers to frequently asked questions on property appraisal on the comptroller's website. One of the questions listed inquires what an appraisal district should do when a majority of sales in a market area are foreclosure sales. The comptroller notes that foreclosure sales may not meet the definition of an arm's length transaction and may or may not represent market value. The comptroller advises that such sales should be compared to other sale transactions to determine whether the prices are a good indication of value and states that an appraisal district "must consider foreclosure sales" in appraising residence homesteads, according to Section 23.01(c), Tax Code.

The question has arisen whether the guidance provided by the comptroller's office regarding the use of foreclosure sales to determine the market value of residence homesteads is consistent with Section 23.01(c), Tax Code. It has been argued that the comptroller's Summary

of the International Association of Assessing Officers Standard on Sales Verification conflicts with Section 23.01(c) and that some appraisal districts, relying on the comptroller's guidance, are following the comptroller's summary rather than the Tax Code.

The comptroller's property tax assistance division opined in an e-mail to a member of my staff that H.B. 1038 does not require that foreclosures be included in developing models for the appraisal of similar properties. The bill merely provides that they may not be excluded. Foreclosure sales that comply with the definition of "market value" in the Tax Code (i.e., sales that involve an arm's length transaction, property that is on the market for a reasonable period of time, a willing buyer and seller, and the like) should be included in appraisal models and are included in the ratio analyses the comptroller's office prepares for the property value study required by Subchapter M, Chapter 403, Government Code. The comptroller's office compares all foreclosed properties in a neighborhood or area to other "regular" sales. If the foreclosure sales are for a similar price per square foot, the comptroller's office uses them as comparables. If the foreclosure sales are for dramatically lower prices than other sales in the same neighborhood or area, the comptroller's office does not use them. The comptroller's office prepares analyses of foreclosure sale prices to ensure that the office uses them in its models appropriately and suggests that appraisal districts do the same.

The comptroller's property tax assistance division argued in a subsequent e-mail that the bill and the International Association of Assessing Officers standards do not conflict. According to the e-mail, the law prohibits excluding foreclosure sales but does not permit them to be used in appraising property if they do not meet the definition of market value. The comptroller's office has advised appraisal districts to consider foreclosure sale prices and use them if they are comparable to regular sales prices after an analysis of the terms of sale and other factors. The e-mail stated that the legislature could require that foreclosure sales be used regardless of the terms of the sale but that such an approach would violate appraisal standards.

The Texas Constitution authorizes the legislature to specify the manner for determining the market value of property for ad valorem tax purposes. The legislature has defined "market value" in Section 1.04(7), Tax Code. That subdivision, and in particular Paragraph (C) of that subdivision, has generally been construed to prohibit using foreclosure sales in valuing property. However, in H.B. 1038, the legislature precluded chief appraisers from excluding foreclosure sales, notwithstanding Section 1.04(7)(C). Testimony in committee and on the House and Senate floors indicated that the bill was intended to prevent appraisal districts from excluding foreclosure sales in valuing property. It was recognized that such sales often result in lower prices than regular sales, but it was argued that as a matter of fairness and in an effort to ascertain the true market value of property, sales at low prices as well as sales at high prices should be considered. In light of that intent, are chief appraisers categorically required to take foreclosure sales into consideration in appraising residence homesteads or may they exclude them if they determine, based on the sales price or other factors, that they were not for market value?

The Honorable Greg Abbott

December 13, 2011

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Thank you in advance for your consideration of this matter. Please do not hesitate to contact me if you need any additional information regarding this request.

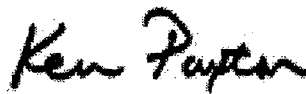
Sincerely,



Kevin P. Eltife  
State Senator  
Chair, Senate Committee on Administration



Dan Patrick  
State Senator



Ken Paxton  
State Representative