

# MINNESOTA · REVENUE

## Minnesota Department of Revenue 2012 Sales Ratio Study Criteria

### Special Notes

#### **Forward-Adjusted Methodology Transition**

In the 2012 sales ratio study, the Department of Revenue will use a forward-adjusted methodology to calculate ratios for the State Board of Equalization. This process will adjust the sale prices forward to January 2013 and match the sales to the preliminary 2013 assessors' estimated market values to calculate ratios for the 2013 State Board of Equalization. The new methodology is intended to encourage assessors to set estimated market values to current market conditions and bring the State Board of Equalization ratios more in line with the Tax Court ratios. More details on the new methodology and its impact on valuations can be found on the department's website. Contact the sales ratio unit with any questions or for more information.

#### **Computerized CRV Submission**

The Department of Revenue encourages all counties to become involved with submitting computer files of certificates. In 2011 all 87 counties submitted their sales data electronically. Counties are also piloting the electronic certificate of real estate value (ECRV) process. The department needs to receive a timely flow of certificates in order to meet the January 15, 2013 deadline for completing the 2012 sales ratio study. The computerized certificate of real estate value process allows us the chance to produce a much better study in the short time we have available.

#### **Agricultural study classes**

The 2008 legislative session changed the method of classifying agricultural property from farm and timber to productive and non-productive classes. This required changes to sales ratio property class reporting. The changes are described in the Special Problem Sales addendum to the criteria found on page 10. The changes should be fully implemented now.

#### **State Board and Tax Court Studies**

These criteria will be used for the Department of Revenue's sales ratio studies conducted in 2012. The studies prepared for the 2013 State Board of Equalization and 2012 Tax Court will use sales that occur between October 1, 2011 and September 30, 2012. These sales will be matched with the 2012 assessors' estimated market values for the Tax Court and to the preliminary 2013 assessors' estimated market values for 2013 State Board of Equalization.

#### **School Aids and Local Government Aids Studies**

The 2012 school aids and local government aids studies will use sales that occur between January 2, 2011 and September 30, 2012. The 2011 sales will be matched with the 2011 assessors' estimated market values. The 2012 sales will be matched with the 2012 assessors' estimated market values.

**Sales Submission Dates**

All sales filed with the county auditor's office by October 31, 2012 will be considered for the 2012 sales ratio study. These sales must be forwarded to the Department of Revenue or available for pickup by the regional representative no later than November 15, 2012. This cutoff date is necessary to allow county assessors and regional representatives sufficient time to review the sales for the 2012 study.

**Change of use sales**

Change of use sales will continue to be subject to more review. Buyers and sellers may indicate a use change that does not move a property from one legal class to another, making the sale valid for the study (See page 5).

## Uses of the Department of Revenue's Sales Ratio Study

There are five primary uses of the sales ratio study. They are:

1. The Minnesota State Board of Equalization uses the 12-month study to judge overall levels of assessment. The median ratio is used. The study adjusts sales forward to the January following the sales period to estimate what the ratio would be if the sales data were applied to the proposed assessors' values. The ratios are used to equalize values to enhance uniformity across property types and between jurisdictions.
2. The Minnesota Tax Court uses the 12-month study in property valuation cases. The Tax Court also uses a 9-month study in property valuation cases. The 9-month study uses January through September sales and is preferred by the Tax Court if there is an adequate sample of at least six sales because all sales in the 9-month study occur after the assessment date. The study is used to measure unequal levels of assessment (called discrimination) within property types. The Tax Court uses the median ratio to measure assessment equity. Sale prices are adjusted to the January within the study period.
3. The department's State Assessed Property Unit uses the 12-month study to equalize railroad and utility values. The median ratio is used.
4. The 21-month study is used to produce adjusted net tax capacities for school aid and state aid calculations. The median ratio is used for all aid calculations. This was the original use of the sales ratio study. The adjusted net tax capacity is also used for levy apportionment.
5. Bonding companies use the adjusted estimated market values of cities and towns to measure fiscal capacities for bond rating calculations.

## **Methodology**

The 2012 sales ratio study is based on the guidelines described in the International Association of Assessing Officers' (IAAO) *Standard on Ratio Studies*, January 2010. The sales acceptance or rejection rules for the 2012 study are similar to those used on previous studies.

### **Financing**

All sales in the 2012 study will be reviewed to see if adjustments for financing are needed. Sales recorded on contract for deed or sales recorded on warranty deeds that include an assumption of an existing mortgage or a seller-provided mortgage will be adjusted. Financing adjustments will not be made to new mortgages from third parties.

### **Time**

Time adjustments will be made to adjust selling prices to the appropriate assessment date for each study. Time adjustment factors developed from sales in a region will be tested to ensure that they are statistically significant. If no significant time trend can be found, the sales prices will not be changed for time. Whenever possible, time adjustment regions will not be larger than a county.

### **Stratification**

In the state board study only, stratified sales ratios will be reported for residential and seasonal residential property in areas individual strata contain at least 6 sales; otherwise, only city/town ratios and countywide ratios will be reported.

### **Verification**

The terms of sale should be verified. The Department of Revenue does not verify residential or seasonal recreational residential sales. These sales are processed by clerical screening and computer edits. All of the normal rejection criteria apply to these sales. In addition, residential and seasonal residential sales recorded on probate deeds, quit claim deeds and sales involving estates are automatically rejected unless the county assessor has notified the department's regional representative that all such sales will be verified. The regional representative must agree with the verification before these sales will be used.

The Department relies on county verification of sales subject to review of the procedures and processes used by the county. All sales of income properties are reviewed.

### **Special Assessments**

In most cases, special assessments should be ignored. They usually involve long-term encumbrances to the property that will lower ratios. Including special assessments can complicate the determination of sale prices without significantly improving the study's accuracy. Special assessments should be included in the sale price only if the dollar amount of the assessment is included in the consideration and the cost of the assessment has contributed value that has been included in the current year assessor's estimated market value.

## Guidelines for Accepting or Rejecting Sales

The Minnesota Department of Revenue's sales ratio study follows IAAO guidelines. These guidelines are described in *The Standard on Ratio Studies*, IAAO January 2010. The IAAO guidelines have been modified in some cases to meet peculiarities of the Minnesota property tax system.

All open market arms-length sales should be accepted for the study. An "open-market sale" is one in which the buyer and seller are acting prudently, and the price is not affected by undue stimulus. Neither the buyer nor the seller must be under great pressure to complete a transaction in a short time. An "arms-length sale" is between two parties, both of whom are seeking to maximize their gain from the transfer.

The sale price should reflect only the price paid for the real estate that was transferred. If part of the purchase price was for personal property or the business rights, the price should be adjusted. All adjustments must be documented.

### Reject Criteria

The following list spells out the general types of sales that do not meet the acceptance criteria and should be rejected for the study.

1. **Old sales (sales before the study period).** Note that the study period for school aids is longer than the period for equalization. An old sale is one that occurred before the start of the school aids study. For this year, the school aids study begins January 1, 2011. Use reason 14 for payoff of a contract for deed.
2. **Sales between related individuals or corporations.**
3.
  - a. **Sales involving governmental agencies as buyers or sellers of property or all sales involving public utilities (including railroad and pipeline companies).**
  - b. **Sales involving charitable, religious or educational institutions.**
4. **Partial-interest sales.** *These are sales of less than the total interest of the property.* If more than one sale occurs and the combined sales equal the total interest, the sale could be used. See page 10 for a discussion of income properties involving splits or combinations that equal the total interest.
5. **Sales involving change of use from one legal property class to another will be reviewed.** Change from residential to commercial would be an example of this type of use change. However, a change of use would not be involved if a restaurant were converted to an office building since both would be classified as commercial property. One exception to this is a change of class from seasonal-recreation residential to residential or vice versa. These sales will be used. Also sales of 34.5 acres or more will not be automatically excluded if the class changes are among the agricultural, residential, seasonal-recreational, or managed forest classes. The property will remain in the class it was in before the sale. Use change requires that most of the value will be moved to a different property classification.
6. **Unusual financing.** This includes sales that have non-monetary consideration and sales that have terms that result in extremely large financing adjustments. These would include:
  - a) Zero interest payments for a long period.

- b) Extreme interest rates that make the finance adjustment become a large part of the sale price and move the sale into the extreme ratio range.
  - c) Income guarantees that require the seller to pay the buyer money if a specified income is not realized from the property.
- 7. Sales of incomplete or partially assessed structures.** Sales should be rejected if the property was substantially improved between assessment date and sale. The change must exceed five percent of the previous year's market value. Property damaged between assessment date and sale also should be rejected due to physical change. The intention is to include sales in which the physical change is merely cosmetic or would not have caused the assessor to change the market value of the property. Sales involving structures that are more than 5% incomplete *may* be excluded.
- 8. Sales of convenience to correct defects of title or change the character of the title.**
- 9. a. Trades of properties or transfers in which nonmonetary items, such as stocks, bonds, or personal property is used as the medium of exchange.**
- b. Sales by representatives of estates to members of the immediate family.**
- c. Sales to a trustee for the benefit of some beneficiary.**
- d. Estate sales not exposed to the open market.** Transactions of residential or SRR properties using a personal representative or conservator's deed are automatically rejected. Sales of other property types are subject to verification and may be included. If a property is sold by the heirs after probate, the sale must be verified.
- 10. Prior interest, such as lease with option to buy.**
- 11. Skipped crv number.** Used to indicate that auditor's number was not used.
- 12. Unique reject reason that Department of Revenue Regional Representative must authorize.**
- 13. Duplicate crv.** Buyer and seller each file a certificate for the same parcel. This code is also used in the Department of Revenue duplicate edit.
- 14. Sale of interest in or payoff of a contract for deed or mortgage assumption.**
- 15. a. Sales to avoid foreclosure such as short sales or sales back to the bank.**
- b. Sales involving legal actions such as foreclosures, divorces, bankruptcies and sheriffs' sales.** To be automatically rejected, a sale must be ordered by a court. All other sales must be verified.
- 16. a. Splits of property not classified as agricultural, rural vacant land, or managed forest.**
- b. Splits, less than 34.5 acres, of agricultural, rural vacant land, or managed forest.**
- c. Splits, greater than 34.5 acres, of agricultural, rural vacant land, or managed forest when the assessor's value is not available for the necessary study years.**

**17. a. Sales in which a significant but unknown portion of the total price is non-realty (personal property - franchise fees - etc).**

**b. Sales in which there is a significant known amount (50% or more) of non-realty included in the sale price (personal property - franchise fees - etc). If the sale includes a large but well-documented non-realty portion, it may be used in the sales ratio study.**

**c. Sales of non-assessed property such as cemetery lots.**

**18. “Sales” which actually are rewrites of the terms of a contract for deed.** If rewrite occurs within a year of the original contract, both will be deleted. If it is more than a year, the original sale will be used.

**19. Sales involving employee transfer or relocation using a relocation company.**

**20. Sale - Leasebacks.** Property is leased back to seller. This does not include short-term leases such as to get crops harvested.

**21. Bank sales** are any sale from a bank, HUD, FMHA, or any governmental lending institution to a private party. These sales will be considered for use in the study only in areas where they are so prevalent, they mirror the actions of buyers and sellers of non-foreclosed property. Thorough verification is mandatory before consideration will be given by the Regional Representative to use these sales.

**Resales** of repossessed property may be considered for use in the study. Thorough verification is essential before using these sales. They should only be used if the sale meets the “open market arms-length” test. Resales of repossessed property by lending institutions will not be adjusted for financing terms.

**22. Contract for deed sales with less than minimum down payment unless the verification proves that the chance of default was extremely low or the term is one year or less.** The minimum down payment for the sales ratio study is 5 percent. Many warranty deed sales, especially residential sales with nominal down payments are usually insured loan sales, and the buyer is considered a good risk. No down payment can be an acceptable form of financing on a warranty deed sale.

**23. Sales of real estate for less than a minimum price.**

<u>Property Type</u>	<u>Minimum Price</u>
All bare land sales.	\$3,000
All other property.	\$10,000

- 24. Sales in which the property is located in more than one county. Sales of property located in more than one taxing jurisdiction which do not have separate appraisals for the components of the sale may be excluded.**
- 25. All sales enrolled in Agricultural Preserve and sales subject to minimum assessment agreements in which the sales price is less than the minimum assessment agreement.**
- 26. Sales of doubtful title or other non-arms-length or non-typical market transactions.** For example, sales that are not advertised, listed or promoted to potential buyers (See Addendum).
- 27. Sales with court ordered value that do not involve post sale stipulations or abatements.** The estimated market value (and limited market value) to be used in calculating sales ratios shall be the value established by the assessor before any stipulations or abatements resulting from appeals by property owners. Sales with court established values that were not the result of pretrial stipulations or abatements are not used in the sales ratio study.
- 28. Sales of nursing homes or sales of mobile home parks.**
- 29. Sales with allocated sale prices.**
- 30. Assessor's value limited by Plat Law in the first year.**
- 31. Assemblage.** Properties bought by one buyer to put together a package for later development or change.

## Extreme Ratios

**No sales will automatically be rejected solely because of extreme ratios.** Extreme ratios, whether high or low, are not a valid reason for rejecting or accepting a sale. The extreme ratio usually indicates a sale where extra verification is required. The extreme ratio could be the result of either an error on the certificate, physical change to the property, or a processing error. If the extreme ratio resulted from a data error, the sale could be used after the corrections were made. If the corrected sale still has an extreme ratio, additional verification should be attempted. The sales with the most extreme ratios will be flagged for further review by the regional representatives. The *2010 Standard on Ratio Studies* addresses the extreme ratio problem in section 5.2 Outlier Ratios. IAAO acknowledges that outlier sales can cause distortion, especially when the sample is small. **The Department of Revenue will flag outlier sales but will not automatically remove these sales from the study.**

We will use the IAAO Standard as a means of identifying the outlier sales. We have developed a table of ranges based upon the 2010 sales ratio study to identify the outlier sales. In the 2012 study, the following boundaries will be used statewide to look for outlier sales:

<u>Property Type</u>	<u>Limits of Normal Ratio Range</u>
Residential	65% to 135%
Apartments	65% to 135%
Seasonal Residential	65% to 135%
Farms	65% to 135%
Commercial-Industrial	65% to 135%

The limits are approximately 2 to 3 standard deviations from the mean ratio and 2 to 3 coefficients of dispersion from the median ratio. Statewide, only 5% to 10% of the sales are outside the ranges and flagged on preliminary sales listings.

For the State Board of Equalization proceedings we have established trimming ranges for calculating the coefficient of dispersion. Sales with ratios less than 65% or over 135% are not used to calculate the coefficients of dispersion. The outliers are not used in the calculation because single sales with extreme ratios will distort the coefficients of dispersion.

## Special Problem Sales

### Non-Agricultural Bare Land Sales

Non-agricultural bare land sales will be included in the study for the State Board of Equalization. Non-agricultural bare land sales are not included in any state aid ratio studies (M.S. 124.2131 subd 1b). Special codes will be assigned to land sales so they may be identified and studied.

### Agricultural and Bare Land Sales

The 2008 Legislature changed the way agricultural property is classified. The changed class structure should have been fully implemented by 2011. The class structure is based upon productive (2a) and non productive (2b) land. Future sales ratio studies will have three agricultural groupings: all productive (2a), all non-productive (2b) and a combination of lands group, (2a) with (2b). The combined 2a-2b study will be the primary study for the State Board of Equalization. In order to implement the new structure we will require additional information about each sale. The new information includes the number of acres of tillable land, pasture land, woods, meadow, and waste land in each sale. Since in many parts of the state most sales will include a mixture of 2a and 2b lands, the acreage detail will allow us to group the mixed sales into proper studies for additional analysis. Initially sales that are entirely classified as 2a should be coded as a PT 31 or 32 if they are 34.5 acres or more or a PT 36 or 37 if less than 34.5 acres; sales that are entirely comprised of 2b lands should be coded as a PT 33 or 34 if they are 34.5 acres or more or a PT 38 or 39 if less than 34.5 acres; and all mixed sales (comprised of 2a and 2b) should be coded as a PT 47 or 48 if they are 34.5 acres or more or a PT 49 or 50 if less than 34.5 acres.

New property classes and PTs for the sales ratio study are:

Ag Class 2a land w/ bldgs (34.5 or more acres)	31
Ag Class 2a bare land (34.5 or more acres)	32
RVL Class 2b land w/ bldgs * (34.5 or more acres)	33
RVL Class 2b bare land (34.5 or more acres)	34
Managed Forest Land Class 2c (34.5 or more acres)	35
Ag Class 2a land w/ bldgs (less than 34.5 acres)	36
Ag Class 2a bare land (less than 34.5 acres)	37
RVL Class 2b land w/ bldgs * (less than 34.5 acres)	38
RVL Class 2b bare land (less than 34.5 acres)	39
Managed Forest Land Class 2c (less than 34.5 acres)	40
Mixed Ag Class 2a & RVL w/ bldgs (34.5 or more acres)	47
Mixed Ag Class 2a & RVL bare land (34.5 or more acres)	48
Mixed Ag Class 2a & RVL w/ bldgs (less than 34.5 acres)	49
Mixed Ag Class 2a & RVL bare land (less than 34.5 acres)	50

\* = RVL property can only have a minor, ancillary structure to still qualify for this PT Code.

Split Sales of 2a, 2b, and 2c lands consisting of at least 34.5 acres which were sold off will be considered for the study.

An example would be a situation in which a farmer sells off 40 acres from a 160-acre farm.

County assessors are asked to make sure that value is split promptly after the certificate of real estate value is filed to assure uniform treatment of split sales throughout the state.

Non-agricultural split sales should not be used.

### **Commercial and Industrial Sales**

Whenever possible, we are required to calculate separate ratios for commercial and industrial property. However, in most areas we will have to use a combined C&I ratio due to the small number of industrial sales.

## **Tests for evaluating reject Code 26 – Sales of doubtful title or other non-arms-length or non-typical market transactions**

In the Minnesota Department of Revenue's 2012 Sales Ratio Criteria, it states in the Guidelines for Accepting or Rejecting Sales, that "All open market arms-length sales should be accepted for the study. An "open market sale" is one in which the buyer and seller are acting prudently, and the price is not affected by undue stimulus. Neither the buyer nor the seller must be under great pressure to complete a transaction in a short time. An "arms-length sale" is between two parties, both of whom are seeking to maximize their gain from the transfer."

Under the Reject Criteria, the Guidelines go on to spell out the general types of sales that do not meet the acceptance criteria and should be rejected from the study. Rejection Code 26 states that "Sales of doubtful title or other non-arms-length or non-typical market transactions." should be rejected from the study. It further states, "For example, sales that are not advertised, listed or promoted to potential buyers".

While Reject Code 26 is a valid code, a blanket application of rejecting all sales that are "not advertised, listed or promoted" would reject many sales that still meet the DOR's guidelines of sales that are open market and arms-length.

In an effort to maximize the number of sales in the ratio study sample and to provide appraisers with all possible sales that reflect market value, market trends, and help to establish benchmarks for current and future assessments the following three tests have been developed to determine if the sale should be rejected as a Reject Code 26 or accepted on its merits and included in the ratio study. Transfers with doubtful title should be rejected with RC # 26.

**Test #1.** Was the sale exposed to the market, or announced, and /or promoted through realtor listings, newspaper or other publications, advertisements, brochures or other promotional or informational mailings, including if the property was For Sale by Owner (FSBO)?

If the answer is **YES**, the sale **SHOULD NOT** be rejected as a Reject Code 26.

If the answer is **NO**, go to Test #2.

**Test #2.** Was an appraisal done prior to the sale to establish the sale price or used as a starting point for negotiations?

If the answer is **YES**, the sale **SHOULD NOT** be rejected as a Reject Code 26.

If the answer is **NO**, go to Test #3.

**Test #3.** Did the sale involve a willing and informed buyer and a willing and informed seller under no duress to buy or sell and is the sale price typical of the market for this type of property in your assessment district?

**Note:** If through the verification process, it is determined that the sale should be considered as a market comparable and meets all other acceptance criteria, then the sale should be include in the study.

If the answer is **YES**, the sale **SHOULD NOT** be rejected as a Reject Code 26.

If the answer is **NO**, the sale **SHOULD** be rejected as a 26.

**Note:** The Reject 26 code is currently not an allowable reject code for Agricultural sales, Apartment sales, and C/I sales just because the property was not advertised. But, individual situations may warrant the use of the Reject Code 26 on these property types.

There will always be some highly unusual or questionable sales that you will encounter. It may be very difficult to determine if the sale should be a Reject 26 or not. Any questions concerning whether a sale should be rejected as a 26 or included in the study as a good sale should be reviewed with your county assessor and your Regional Representative.

A sale with a Reject Code 26 with no explanation will not be accepted. Additional documentation will be required.

## **Methodology for Time Adjustment Appeals to the Sales Ratio Study**

All sales used in the sales ratio study are adjusted for time and terms. The standard time adjustment procedure is ratio trending over time. The sales are run through a regression routine to produce a time trend line for the study period. If there is no correlation between the ratios and time at the 90 percent confidence level, no time adjustment is made.

The fact that no time adjustment is applied using standard procedures does not mean that prices are not changing in an area. It means that the price-level change is not systematic or consistent over the period being tested. IAAO recognizes four methods of calculating time adjustments:

1. Paired Sales Analysis
2. Resale Analysis
3. Sales Ratio Trend Analysis
4. Multiple Regression Analysis

The department uses the third method (Sales Ratio Trend Analysis) because the necessary data are readily available. Data necessary for the other methods are not available at the state level.

If a county feels that the time adjustments are not representative of local markets, it has the right to appeal. If the county is able to show that another method will result in a more accurate time adjustment, the department will review the county's work. If the county can provide additional data, it will be considered.

## Time Adjustment Appeal Procedure

All sales will be time adjusted using the IAAO Sales Ratio Trend Analysis method. If a county disagrees with the adjustment they have the right to appeal. We will use the following time adjustment appeal procedure:

1. The county assessor must notify the Department of Revenue regional representative for that region and the Sales Ratio Unit of the disagreement. The county assessor must list the specific cities, townships, and/or other breakdown of sales that are covered by the appeal and the reason for the appeal.
2. If the county is appealing the appropriateness of the method used to calculate the adjustment, the county assessor must describe what method of time adjustment will instead be used to calculate the time adjustment. This method must be one recognized by the IAAO in the most current *Standards on Ratio Studies* as a valid time adjustment calculation methodology. These include Paired Sales Analysis, Resale Analysis, Sales Ratio Trend Analysis, and Multiple Regression Analysis.
3. The county assessor must provide supporting documentation to the regional representative for review.
4. The regional representative will review the documentation and forward it to the Regional Representative Supervisor. The regional representative will recommend whether to proceed with the appeal based upon the documentation provided by the county.
5. If the regional representative recommends making a time adjustment, the Sales Ratio Unit will recalculate a time adjustment for the region based on the data provided by the county.
6. If the regional representative does not recommend making a time adjustment, or does not have the facilities to analyze the data provided by the county, the county may appeal the recommendation to the Regional Representative Supervisor. The appraisal supervisor will give the county appeal to the Sales Ratio Unit, which will analyze the documentation and recalculate a time adjustment if the material indicates that an adjustment is needed.
7. If the appeal results in a time adjustment, the adjustment factors will be applied to the appropriate sales ratio study uses.

Sales Ratio Unit  
Property Tax Division