

DEPARTMENT OF TAXATION

Division of Assessment Standards

Performance Audit Program Definition

DIVISION OF ASSESSMENT STANDARDS

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Purpose, Authority, and Responsibility

The purpose of the Performance Audit Program is to objectively analyze local government effectiveness related to administration of the property tax system in the State of Nevada by each of the 17 counties. The Department of Taxation (Department) instituted the Performance Audit Program in furtherance of the authorities and responsibilities of the Department, the State Board of Equalization and the Nevada Tax Commission for oversight of the Nevada property tax system. The authority for the Performance Audit Program is derived from Nevada Revised Statutes (NRS) and Nevada Administrative Code (NAC), including but not limited to the following:

NRS 360.200 *“The Department may exercise the specific powers enumerated in this chapter and, except as otherwise provided by law, may exercise general supervision and control over the entire revenue system of the State of Nevada....”*

NRS 360.215(2): *The Department shall consult with and assist county assessors to develop and maintain standard assessment procedures to be applied and used in all of the counties of the State, to ensure that assessments of property by county assessors are made equal in each of the several counties of the State. These procedures must include uniform methods for: (a) Assessing, projecting, and reporting construction work in progress and other new property; and (b) Counting and reporting housing units.*

NRS 360.215(6): *“The Department shall continually supervise assessment procedures which are carried on in the several counties of the State and advise county assessors in the application of such procedures. The Department shall make a complete written report to each session of the Legislature, which must include all reports of its activities and findings and all recommendations which it has made to the several county assessors, and the extent to which the recommendation have been followed.”*

NRS 360.250(2)(a): *“The Nevada Tax Commission may confer with, advise, and direct county assessors, sheriffs as ex officio collectors of licenses and all other county officers having to do with the preparation of the assessment roll or collection of taxes or other revenues as to their duties.”*

NRS 361.333 (1)(b)(2) requires the Department to *“Publish and deliver to the county assessors and the boards of county commissioners of the counties of this state a determination whether each county has adequate procedures to ensure that all property subject to taxation is being assessed in a correct and timely manner.”*

Overview

Although county government has the primary responsibility for local property tax assessment, the State has a public policy interest in promoting fair and equitable assessments throughout Nevada. This public policy is enumerated in the State Constitution and various statutes and regulations. Determination of compliance with this public policy is accomplished through a system of quality control of local performance. Quality control can be accomplished through various processes, including but not limited to ratio studies, procedural/office overviews, and performance audits.

The authorities and responsibilities for the quality control system were discussed in the previous section. The Department historically fulfilled its responsibilities for quality control through the annual ratio study and procedural audit / office review processes.

The Department annually conducts a Ratio Study pursuant to NRS 361.333 and produces a “Report of Assessment Ratio Study” as required by NRS 361.333 and NRS 360.215(6). The annual “Report of Assessment Ratio Study” is used for the equalization process¹ and for reporting on the adequacy of each county’s work practices or procedures.

In the past, the annual “Report of Assessment Ratio Study” included two sections as follows.

1. The first section was the ratio study which is a statistical analysis designed to study the level and uniformity of the assessments. The ratio study is a quality control technique designed for mass appraisal. Generally speaking, a “ratio study” is designed to evaluate appraisal performance by comparing the estimate of assessed value produced by the assessor on each parcel in the sample to the estimate of taxable value produced by the Department’s independent appraisal of each parcel in the sample. The comparison is called a “ratio.” If the “ratio” does not meet certain criteria, processes² occur to adjust values. NRS 361.333(2) permits the Department to conduct a ratio study on smaller groups of counties instead of the entire state in any one year. Therefore, ratio studies are not done on all 17 counties in Nevada in each year. Instead, the Department developed a three year cycle in which approximately 1/3 of the counties were studied each year. Therefore, over the course of three years, all counties are subject to the ratio study quality control process.
2. The second section was a Procedural Audit / Office Review summary designed to document procedures used by County Assessors to discover, value, and assess all

¹ If inequity or bias is discovered, NRS 361.333 provides the Nevada Tax Commission the authority to apply factors designed to correct inequitable conditions to classes or property or it may order reappraisal, the goal of which is to determine whether all real and personal property is assessed at 35% of taxable value. [2009-2010 Report of Assessment Ratio Study, page 2]

² For a full discussion of the processes that occur, please see the annual “Report of Assessment Ratio Study” and the publication entitled “Nevada Property Tax: Elements and Application” published by the Nevada Department of Taxation-Division of Assessment Standards. These are available on the following web site: <http://tax.state.nv.us>

real and personal property within the jurisdiction of the County Assessor. The primary tools for conducting the Procedural Audits / Office Reviews were questionnaires and observation of sample property files. The Procedural Audits / Office Reviews were performed on the counties selected for the ratio study resulting in Procedural Audits / Office Reviews of approximately 1/3 of the counties each year. Over the course of three years, all counties were subject to the Procedural Audit / Office Review as a quality control process.

The Department determined that the ratio study process as previously designed and conducted is a good quality control process and is required by statute. Therefore, the Department will not significantly change this process. The Department will continue independent appraisals and statistical analysis of the results. The results will be reported in the annual "Report of Assessment Ratio Study." The statistical analysis will continue to cover approximately 1/3 of the counties each year as allowed by NRS 361.333(2).

The Department determined that the quality control processes of the annual Procedural Audits / Office Reviews could be strengthened through implementation of this Performance Audit Program. The Procedural Audits / Office Reviews conducted over the last three years created a valuable "baseline" study of all 17 counties over many different operational areas. The Performance Audit Program is designed to provide a much more in depth analysis of specific areas of operations. The Performance Audit Program will use this "baseline" information as a starting point for the more in depth analyses.

Because the goal of the Performance Audit Program is a more detailed analysis of specific areas of operations in each county, each separate project undertaken in the Performance Audit Program will generally involve all 17 counties, instead of just the counties selected for the ratio study. In addition, the Performance Audit Program will be conducted throughout the year, not just when the ratio study is performed. Therefore, each separate performance audit project undertaken will be reported in a separate, detailed report. The dates that reports are issued will depend on the completion of the project.

Topics will be selected for performance audits based on assessment of risk, current circumstances, significance, and cost/benefit analysis. The Department intends to maintain an Audit Survey or Strategic Planning Process to prioritize and schedule performance audits, within the limitations of available resources. See a sample Strategic Planning (Audit Survey) document attached as Exhibit B.

Even though the Performance Audit Program is somewhat separate from the statistical ratio study, both are quality control processes that enable the State to exercise proper oversight of local governments in the area of tax administration. Therefore, the recommendations of prior Procedural Audits / Office Reviews and the findings of subsequent Performance Audits will be reported annually in the "Report of Assessment Ratio Study" in order to satisfy the requirements of NRS 361.333 (1)(b)(2) and NRS 361.215(6). The status of recommendations or findings will be reported annually until the recommendation either no longer applies or has been implemented. No further

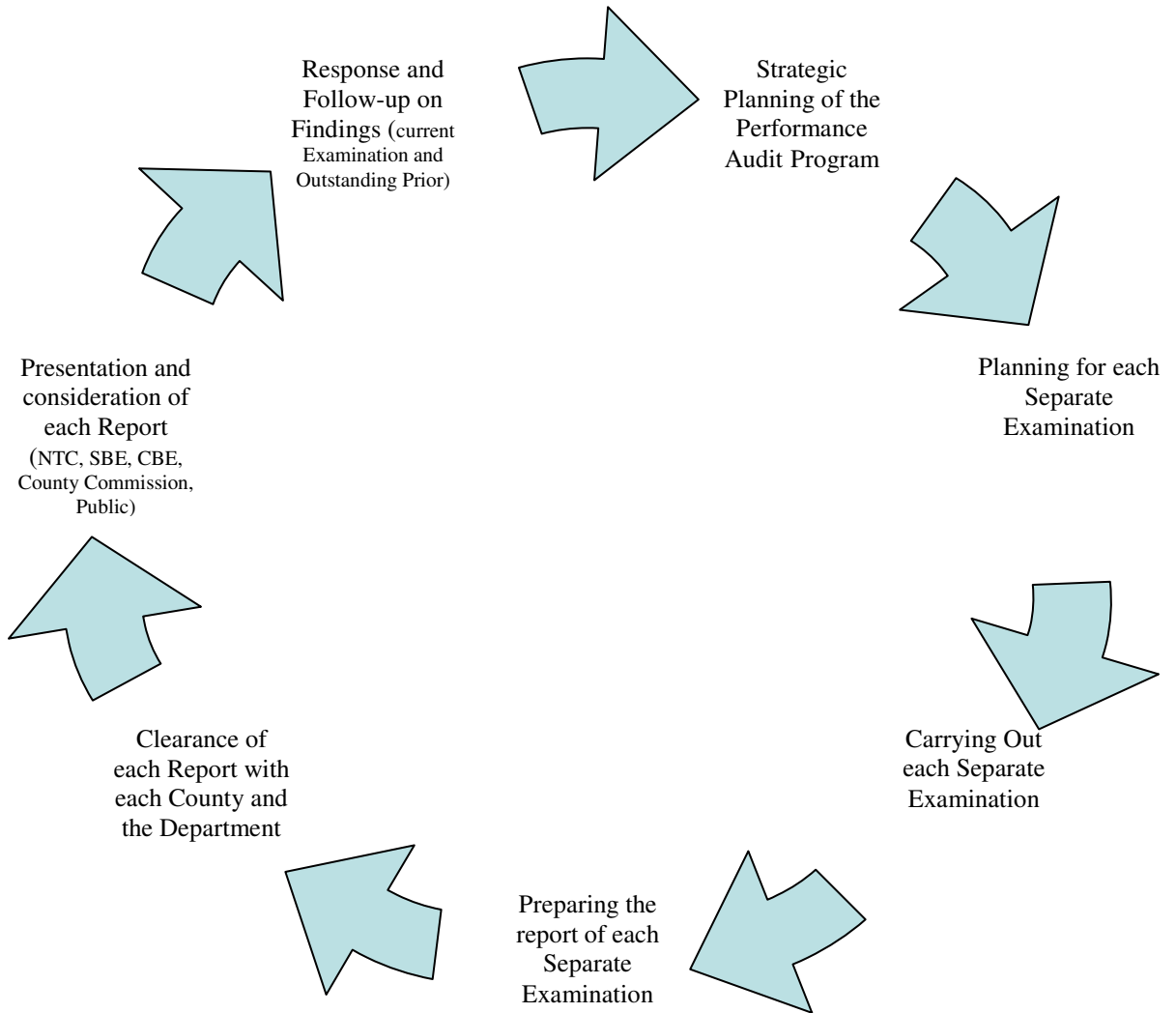
Procedural Audits / Office Reviews will be conducted; however, changes in the baseline data will be noted during the entrance conference for each subsequent Performance Audit to identify issues.

The Department elected to conduct performance audits in compliance with Generally Accepted Government Auditing Standards (GAGAS) issued by the United States Government Accountability Office (GAO). For performance audits performed in accordance with GAGAS, chapters 1 through 3 and 7 and 8 apply to the Performance Audit Program. See Appendix A for a general discussion of performance auditing.

In summary, the annual "Report of Assessment Ratio Study" document will look the same for the ratio study portion and will look different for the Procedural Audits / Office Reviews and Performance Audit portion. Both sections are reports on quality control. The ratio study portion will continue to cover about 1/3 of the counties each year. The Procedural Audits / Office Reviews and Performance Audit portion will be an annual report on the status of outstanding recommendations and/or findings of prior Procedural Audits / Office Reviews or Performance Audits.

Performance Audit Cycle

The elements in each performance audit study can be grouped into three major phases, namely **planning, examination, and reporting**. The performance audit cycle can be summarized as follows:



Program Steps

Step 1 – Strategic Planning (Audit Survey) Process

The strategic planning or audit survey process will assist in determining when and what to audit as well as obtaining a clear understanding of the objectives, work to be done, and the report to be issued. The strategic planning process consists of identifying areas for audit and obtaining basic information and data for use in planning and conducting audits. The current strategic planning process is included as Exhibit B. The initial projects included in the Strategic Planning (Audit Survey) Process were generated from the 3-7-07 white paper attached as Exhibit C. The projects on the Strategic Planning (Audit Survey) document will be revised as often as necessary.

The Strategic planning process will identify the topic of the next performance audit.

Step 2 – Objective(s)

Upon selection of a topic for audit, the objective(s) of the audit must be clearly defined. The statement of the objective(s) must be neither too broad nor too narrow. In general, the objectives of the program will be (1) to assess compliance with laws, regulations, and generally accepted mass appraisal standards (or other applicable standards), (2) to identify factors inhibiting satisfactory performance, and (3) to identify ways that counties can improve their operations. Another objective of the program may be to report on excellent or exceptional performance that may provide useful information to other county officials.

The specific objective(s) of each performance audit project will be stated in the written plan for each audit.

Step 3 – Defining Audit Scope

The scope is the “boundaries” of the audit that addresses items such as (1) the period covered or the “when”, (2) the number of locations or the “where” and “who”, and (3) the kinds of evidence to explore.

The scope will also define what would constitute a “finding” in the report. A finding would be a material problem that will require submission of a plan of corrective action. The scope will also define what may constitute recognition of excellent or exceptional performance and how disclosure of this information would be useful to other county officials.

Audit scope, major considerations and the rationale for the scoping decisions will be included in the written audit plan for each separate audit. In general, all 17 counties will be included in the scope of each audit. Reasons for any limitations on the scope will be included in the written audit plan for each audit.

Generally, entrance meetings will be scheduled with each county during the scoping phase to document systems and identify kinds of evidence to test later in the audit work phase.

Step 4 – Defining Audit Criteria and Sources

In general, the criteria in each audit will be the particular statutes, regulations, and generally accepted mass appraisal standards (or other applicable standards) related to the subject matter. Other sources of information will be considered, as needed, to define the criteria and the sources of the criteria in the audit.

The audit criteria of each performance audit project will be stated in the written plan for each audit.

Step 5 – Defining the Work to be Done

This part of the planning will include the specific audit methodology to be used to provide sufficient, appropriate evidence to achieve the objectives of the audit. The methodology will result in gathering and analyzing information upon which to base the findings, if any, discovered in the audit.

Each audit will be undertaken only after preparation and approval by Department management of a written Audit Program Guide for the audit work phase of the audit, including audit approach and methodology. The Audit Program Guide will provide a description of the specific audit procedures, work paper references, and identification of the auditor performing each procedure. The Audit Program Guide will contain, at a minimum, the following sections: Background, Statistics, Planning the Audit, Audit Scope, Audit Objectives, a section for each objective (including procedures), and an audit wrap-up section.

Each written Audit Program Guide will identify Department staff and external consultants, if any, including their qualifications and special knowledge or skills. Each written audit plan will include (1) the estimated cost of the audit (staff hours and other costs) (2) the estimated timing for conducting the audit, (3) the key milestones and (4) the main control points. Upon approval of the audit plan, the audit work can begin.

Step 6 – Perform Audit Work

In general, adequate preparation prior to audit work is needed. If interviews are part of the audit work, interview outlines will be prepared. Coordination with the auditee will be made to assure that documents are readily available and the impact on the auditee is reduced. Staff will obtain as much documentation as possible prior to starting audit work. For example, web sites will be thoroughly reviewed so that staff members do not ask questions that are answered on the local government's web site.

The audit approach and Audit Program Guide will determine the nature of audit work.

Step 7 – Defining the Reporting Elements

Following completion of audit work, the evidence will be reviewed and analyzed. Auditor(s), Department managers, personnel in the Locally Assessed Group or other pertinent staff will review and consider preliminary findings. The group will consider all of the elements of a finding as defined in GAGAS.

The report will describe the audit results, recommendations, audit objectives, scope and methodology. Other elements may include descriptions of management controls, view of responsible officials, noteworthy accomplishments, or issues needing further study. If the audit results in a finding, the following elements will be included in the findings section of the report: criteria, condition, effect, cause, recommendation and response.

Step 8 – Drafting and Approval of Report

In general, issues will be discussed with auditees prior to preparation of the first draft of the report so there are no “surprises” when the draft is sent. It is important to have each auditee submit written comments on the report prior to official release of the report and to include each auditee’s written responses in the final report.

Staff will determine the appropriate organization of work papers for administration of the Program in compliance with GAGAS 7.77 which states that the work papers will contain documentation in sufficient detail to enable an experienced auditor, having no previous connection to the audit, to understand the audit documentation. Staff will complete and index work papers prior to preparing the preliminary draft report.

The report format may vary slightly for each audit; however, basic sections will be established. The final report will probably consist of 17 sections, one for each county and a summary section for all counties to facilitate comparison between counties for each reporting element.

The audit methodology section of the final report will essentially be the audit methodology in the planning document presented in the past tense, and corrected for methodology changes that may have been needed after the project started.

The Executive Director of the Department or the Chief of the Division of Assessment Standards must approve the final report. All draft reports and work papers are held confidential until the final report is issued.

Step 9 – Issuance and Presentation of Report

DOAS will arrange for formal presentation of the report to each Board of County Commissioners, each County Board of Equalization, the Nevada Tax Commission, the State Board of Equalization, and others, as authorized by Department Management. The final report will be public information and will be posted on the Department’s web site.

Step 10 – Inputs for Strategic Planning and Annual Report of the Program

The final step of each separate audit may be to provide input into the Strategic Planning (Audit Survey) process for the selection of future audits.

Information obtained during the course of each separate performance audit may affect the planning process for future audits. This information will be used in the Strategic Planning part of the cycle. In addition, the status of findings and the activities of the Performance Audit Program will be published annually in the “Report of Assessment Ratio Study.”

Step 11 – Follow up

Generally, within six months of issuing the final report, and annually thereafter in the “Report of Assessment Ratio Study, the Department will review the status of each counties’ outstanding recommendations.

Appendices

Appendix A - Performance Auditing in General

Generally, performance auditing focuses on determining whether organizations, programs, functions and services are achieving the purposes for which they are authorized and funded and whether they are doing so *economically, efficiently, and effectively*. The Nevada Department of Taxation, Division of Assessment Standards (DOAS) does not control the funding for County programs; therefore, the Performance Audit Program does not include economy and/or efficiency audits. The Board of County Commissioners and various County elected and appointed officials (Assessors, Treasurers, Recorders, Managers and Controllers or Finance Directors) are responsible for determining that the work is performed *economically and efficiently*. DOAS is concerned with obtaining reasonable assurance that the tasks are performed *effectively* and consistently between counties.

Generally Accepted Government Auditing Standards (GAGAS) define performance auditing as follows:

A performance audit is an objective and systematic examination of evidence for the purpose of providing an independent assessment of the performance of a government organization, program, activity, or function in order to provide information to improve public accountability and facilitate decision-making by parties with responsibility to oversee or initiate corrective action.

GAGAS further states that performance audits can include (1) economy and efficiency audits and (2) program audits. The DOAS Performance Audit Program will focus only on program audits for the reasons stated above. However, DOAS encourages local officials to examine economy and efficiency. The results of the Program Audits will be public information and may provide benefit to the counties in economy and efficiency issues.

There are four general standards of performance auditing that DOAS has built into the performance audit program as follows:

1. **Qualifications:** The staff assigned to conduct the audit will collectively possess adequate professional proficiency for the tasks required.
2. **Independence:** The staff members assigned to conduct the audit will be free from personal and external impairments to independence and will maintain an independent attitude and appearance. This means that DOAS personnel are independent of the Counties audited.
3. **Due professional care:** Due professional care will be used in conducting the audit and in preparing related reports.

4. **Quality Control:** DOAS will have an appropriate internal quality control system in place and undergo an external quality control review of the performance audit program once every three years.

There are four field work standards of performance auditing that DOAS has built into the performance audit program as follows:

1. **Planning:** The staff assigned to conduct the audit will adequately plan and document the planning of the work necessary to address the audit objectives through preparation and approval of the Audit Program Guide.
2. **Supervising Staff:** The staff members assigned to conduct the audit will be properly supervised. Initially the program will be conducted by the Auditor in the Department, a licensed Certified Public Accountant.
3. **Obtaining Sufficient Appropriate Evidence:** The Department will obtain sufficient, appropriate evidence through audit work conducted according to the Audit Program Guide. Staff will thoroughly review the evidence in the group “findings review meetings” to provide a reasonable basis for any findings.
4. **Preparing Audit Documentation:** Staff will prepare audit documentation using the uniform system of indexing created as part of the development of the program. The audit documentation will be prepared in sufficient detail to enable an experienced auditor, having no previous connection to the audit, to understand from the audit documentation the nature, timing, extent, and results of audit procedures performed, the audit evidence obtained and its source and the conclusions reached, including evidence that supports the auditor’s significant judgments and conclusions. The audit documentation will support any findings, conclusions, and recommendations in the report.

There are three reporting standards of performance auditing that DOAS has built into the performance audit program as follows:

1. **Form of the report:** Reports will be prepared for hardcopy and electronic distribution.
2. **Report Contents:** Reports will contain (1) the objectives, scope and methodology of the audit (2) the audit results, including findings, conclusions, and recommendations, as appropriate (3) a statement about compliance with GAGAS (4) written responses of county officials and (5) if applicable, the nature of any confidential or sensitive information omitted. Generally, the report will contain a separate section for each county and a summary section allowing comparison between counties.
3. **Report Issuance and Distribution:** The Department will present the report to each county Board of Commissioners (or Board of Supervisors), each county Board of Equalization, the State Board of Equalization and the Nevada Tax Commission. Additional presentations may be made. The reports will be available as public information in hardcopy form and on the Department web site.

The full text of government auditing standards can be downloaded from the GOA site at the following address: <http://www.gao.gov/new.items/d07731g.pdf>.

Appendix B – Strategic Planning (Audit Survey)

Performance Audit Topic	Priority H=High M=Medium L=Low	Circumstances H=Hot C=Cold	\$ Significance S=Small M=Medium L=Large	Cost/Benefit Pass/Fail Not necessarily \$ only	Audit Order
Land Valuation Vacant Improved	H	H	L	Benefits > Costs	1 st
Abatement of Property Tax NRS 361.4722 and 361.4723					
Sales Validation (include in Land Valuation project)					
New Construction					
Marshall and Swift					
Subdivision					
Water Rights					
Agricultural Property (include in Land Valuation Project)					
Personal Property					
Files and File Content					
Manufactured Homes					
Training					
Aircraft and Hangars					
Mapping Systems					
Other	L	C	S	Costs > Benefits	Last or Never

Note: This is merely a sample of the process for prioritizing and selecting topics for the Performance Audit Program. There will actually be a “living document” maintained by the Department to revise priorities, add new topics, consolidate topics, or delete topics for consideration for subsequent performance audits.

Note: The Land Valuation project will be the first performance audit under the program because there is generally consensus in the Department that this is the most important issue currently.

Appendix C – White Paper

Monitoring Appraisal Performance

Background

Nevada assessors estimate the taxable value of properties based on the statutory requirements of NRS 361.227. The viability of Nevada's property tax depends largely on the accuracy of those estimates, because they are the legal basis for the levy of property taxes. Over the last four years, the Tax Commission, the State Board of Equalization, the Department of Taxation, taxpayers and assessors have all expressed concern about the accuracy and uniformity of the appraisals. For instance, when the Lake Tahoe Special Study was presented to and reviewed by the Tax Commission, the Commissioners remarked that, at a minimum, appraisal performance should be monitored; "not just whether each county is legal within what that county is doing specifically, but that there is some degree of uniformity as it's appropriate among the counties."¹ The Commission directed the Department "to do more monitoring for consistency amongst the various appraisers of the state as a part of their ratio factor study."²

One of the concerns expressed at the meeting was, how could the Department find equalization problems at Incline Village and at the same time give Washoe County a "pass" in the ratio study. Part of the answer lies in the ratio study design. The ratio study currently designed is based on the requirements of NRS 361.333, in which the Department is required to compare the median ratio, overall ratio and coefficient of dispersion (COD) for the total property in each of the 17 counties and for each major class of property within each county. The classes of property are identified as improvement values for the reappraisal area, land values for the reappraisal area, and total property values of vacant land, single-family residential property, multi-residential property, commercial, industrial, and rural property in the reappraisal area.

Although the statute requires the statistical analysis for the major classes of property only in the reappraisal area, the Department requested and received approval from the Tax Commission in October, 2003 to expand the ratio study. The problem the Department had identified was that not all types of property were represented in a reappraisal area. In addition, because of the 5 year rotation system used by county assessors for reappraising and the 3 year rotation system used by the Department for the ratio study, it was possible that any given reappraisal area would only be examined once every 15 years. In order to get a more representative study and to ensure all areas were examined during the 3 year rotation, the ratio study was expanded so that a sample could be drawn from all areas of the subject county and for each property type. The minimum sample size for statistical analysis is 6 of each type of property in each reappraisal and non-reappraisal area. A larger sample of each property type is taken if available and as resources of the Department allow. A typical sample size taken by the Department annually is 1,000 to 1,500 properties across 5 or 6 counties.³

As a result of the ratio study requirements, the Department does not stratify property into geographical areas smaller than reappraisal areas. The statutory emphasis is on "types" of

¹ Commissioner Marvel commenting on alternative actions to take with regard to the results of the Lake Tahoe Special Study, NTC meeting 3-13-06, p. 189-190.

² Motion adopted by the Commission, NTC meeting 3-13-06, p. 195, ll. 1-4.

³ The 2006-07 ratio study had 1,077 observations; the 2005-06 ratio study had 1,459 observations.

property within each reappraisal area. Thus it is possible for a neighborhood or community or even a type of property within the reappraisal or non-reappraisal area to experience different market influences or varying appraisal practices that would not be captured by the ratio study. In the Lake Tahoe Special Study, the sample design was strictly on residential property in Washoe and Douglas Counties at Lake Tahoe, a distinct area from the general reappraisal areas within those counties. Property within the Lake Tahoe area showed a statistical result both in median and COD which varied from the statistical results of the reappraisal areas of which the Lake Tahoe area is a part. This is so because the median and COD of the observations within the much larger reappraisal area can overpower the results of observations of the smaller unit within it.

Other states may stratify the ratio study on more narrow geographical areas, oftentimes as narrow as by neighborhood. Such narrow stratification is possible because of the data available. However, most ratio studies are “sales ratio studies,” in which fair market value is the standard. In those states, all sales are collected and may be stratified by any defined geographic area, then compared to the assessor’s estimate of full cash value of the properties within that area. In Nevada, however, taxable value is the standard, in which the land is valued based on full cash value and the improvements on replacement cost new less depreciation defined by statute (RCNLD). Comparing the assessor’s bifurcated land and improvement taxable value to market sales within the neighborhood would only show the effect of the valuation limitation of RCNLD. In order to discover whether the assessor is appropriately valuing property according to RCNLD of the improvements plus full cash value of the land, the Department must independently generate an RCNLD number for comparison. The sample size therefore, is limited to the number of observations the Department can generate through physical inspection and analysis.

County assessors also annually submit land factors for non-reappraisal areas pursuant to NRS 361.260(5). Land factors are developed by comparing the current assessed value of sold properties to the sale price. The ratio of the comparison must fall between 30 and 35 percent of the taxable value of the land. The Department reviews the assessors’ land factors by examining the sales data, analyzing outliers, and calculating various statistics which would indicate how accurate the selected factor is.

Analysis

There are two approaches which might address the Tax Commission’s directive to do more monitoring of appraisal performance. The first approach, and the one more easily implemented, is to enhance the work practices portion of the ratio study. Currently, NRS 361.333(1)(b)(2) requires the Department to make a determination about whether each county has adequate procedures to ensure that all property subject to taxation is being assessed in a correct and timely manner, and to note any deficiencies. The Department staff travel to the offices of county assessors to review the procedures used to discover, value, and assess all real and personal property within the jurisdiction of the county assessor. The Department reviews the resources of the office; reviews a sample of property files; and interviews assessors and their staffs. Departures from required or accepted appraisal practices are noted and recommendations for improvement are made.

At the March 13, 2006 meeting of the Nevada Tax Commission, the Department suggested that the current work practices portion of the ratio study be “beefed up.” The State Board of Equalization has been studying the issue of equalization and also recently heard from the Department about how some other states supplement the ratio study with performance audits. Performance audits provide assurance or conclusions relating to audit objectives that provide an evaluation against objective criteria, such as specific requirements or measures, or statutorily required appraisal and assessment practices. Performance audits provide objective analysis so that those charged with governance and oversight may improve program performance, facilitate decision making by the State Board and/or the Tax Commission, and contribute to public accountability.

There are several appraisal techniques and tools available to assessors to determine the full cash value of land, and even some choices available in the application of the Marshall Swift costing manual when developing RCNLD. Performance audits would require additional work in first identifying the “best practice” for each procedure. The idea of the performance audits would focus on how tasks are carried out – on procedures, not specifically on results. In fact, this idea was introduced to the Assessor’s Association at their September, 2006 conference, and the assessors indicated their willingness to work with the Department on establishing the kinds of information necessary to form an opinion about the “best practice.”

Some development time would be necessary before the Department could carry out the performance audit analysis. Department appraisers would require training in performance audit techniques, “best practices” need to be identified, and priorities established for auditing performance in a variety of areas. The first priority undoubtedly would be best practices in land valuation, but other areas of significant interest include best practices in identifying remainder parcels for application of the property tax abatement, how exemptions are determined, how changes in the law were applied such as open-space treatment of golf courses, and common-area interests.

The second approach is to enhance the ratio study by generating additional observations in more narrowly defined geographic areas. The option would require direction as to how those geographic areas should be defined, the appropriate sample size, and other criteria for the study design. Additional regulations would be helpful in this regard. Enhancement of the ratio study is limited only by Department resources available to increase the sample size.

Action Plan

By the Tax Commission:

- 1.) Prioritize the topics for regulatory consideration. *See Exhibit 1, List of proposed topics.*
- 2.) Determine whether performance audits should be performed by the Department.
 - a.) If yes, consider the time-frame for completion and priority of audit subjects. Should the 3 year cycle be maintained for performance audits or should all counties be subject to

an annual performance audit, based on a limited number of “roll-out” issues? For instance, if the use of alternative land valuation techniques is the “roll-out” issue, should just the current cycle of counties be examined on the one issue, or should all counties?

b.) Consider and approve recommendations for criteria to be used for the performance audit. (See discussion below).

3.) Determine whether performance audits should be performed prior to, concurrently with, or after the rulemaking process.

a.) Should performance audits be performed prior to rulemaking to provide a baseline analysis, or should rulemaking occur concurrently or prior to audits to enhance criteria for performance auditing?

4.) Adopt regulations regarding statistical criteria for the ratio study. Determine whether an expanded database is necessary and/or feasible.

5.) Approve the Manual of Assessment Policies and Procedures as it currently exists. Appoint a blue-ribbon committee comprised of DOAS staff and assessors to work on updates for the Manual. Schedule workshops to review updates as they are prepared.

By the Department:

If performance auditing is approved:

1.) Train Department appraisers in aspects of performance auditing.

2.) Simultaneously research and propose the criteria or “best practices” for procedures relating to areas prioritized by the Tax Commission. *See Exhibit 2 for topics for which “best practices” would be determined.* Criteria provide a context for evaluating evidence and understanding the findings, conclusions, and recommendations included in the report. The criteria should be:

a.) Objective: free from bias

b.) Measurable: permit reasonably consistent assessments, qualitative or quantitative, of subject matter.

c.) Complete: include relevant factors that could change a conclusion about the subject matter; and

d.) Relevant: related to the subject matter.

Possible criteria could include the purpose or goals prescribed by law or regulation; policies and procedures established by the county assessor; technically developed standards or norms; performance of similar entities; and best practices identified by the IAAO.

3.) Recommend level of significance for the work practice. “Significance” is defined as the relative importance of a matter within the context in which it is being considered, such as the

relative magnitude, the nature and effect of the matter, and the needs and interests of intended report users.

4.) Determine what is sufficient, appropriate evidence and documentation to support findings, conclusions, and recommendations.

5.) Prepare audit plan; perform performance audit on designated counties.

6.) Determine reporting standards for performance audits, including descriptions of the objectives, scope, and methodology. Determine the elements of any findings, i.e:

a.) Report the criteria, that is, the required or desired state of what is expected from the assessment program;

b.) Report the condition: what the auditors found regarding the actual situation.

c.) Report the cause: evidence on the factor or factors responsible for the difference between the condition and the criteria.

d.) Report on the effect or the potential effect, preferably in quantifiable terms.

e.) Report the findings including the nature and extent of the issues being reported and the extent of the work performed that resulted in the finding.

f.) Recommend actions to correct problems and improve operations.

If increased database for ratio study is directed:

1.) Design ratio study to encompass more narrow geographic areas pursuant to the priorities established by the Tax Commission.

2.) Plan /shift staff workload to accommodate additional fieldwork.

Exhibit 1 – Proposed Topics for Regulatory Consideration

1. Define land, both physically and legally. In simplest terms, the definition could mean real property exclusive of improvements on the land. This definition could appear as NAC 361.017.
2. Clarify the meaning of improvements and the difference between improvements on the land and improvements to land. NAC 361.188 defines improvements as improvements on the land (“Improvement” means all appurtenances erected upon or affixed to the land), so all references to improvements throughout NRS or NAC, including golf course improvements, could mean improvements on the land.
3. Clarify the difference between vacant and improved land. NAC 316.113 says that “Improved land” means land on which there is an improvement sufficient to allow the identification of or establish actual use. Consequently, one may identify the actual use of land lacking improvements on the land as vacant (land use codes 10-19). Interestingly, Nevada law defines vacant land as a form of improved land.
4. Clarify the meaning of “cost of replacement.” found in NRS 361.227 1(b), which requires revision of NAC 361.128. For example, the cost of an improvement on the land equals its full economic cost, including without limitation the usual laundry list of costs without loopholes. It should also allow assessors to apply unusual condition multipliers if supported by verifiable market data and state explicitly that any modifications to or substitutions for Marshall Swift standard costs must appear on the tax roll as the cost of replacement. Consideration should be given to requiring assessors to submit cost update forms to the Department at least once a year.
5. Resolve the legal ambiguity over the cost date. NAC 361.128 specifies October 1 of the year preceding the closure of the roll. For example, if the 2007-08 roll closes January 1, 2007 the cost date should be October 1, 2006, not October 1, 2005 as the Department does it now. Moving the cost date to July 1 one year prior to the lien date, which coincides with the sales cutoff date, probably makes better sense, but may impose a time crunch on the assessors.
6. State explicitly that the principle of substitution applies to improvements on the land and that replacement cost thus determines the maximum full cash value for any improvement. This could appear as an addition to NAC 361.014
7. Clarify the definitions for the abstraction and allocation methods in NAC 361.107 and 361.109.

“Abstraction method” means a method of estimating the value of land by subtracting from the sales prices of improved parcels the full contributory value of all items attributable to the value of the improvements on the land, thus yielding estimates of the residual or remainder value of the improved land.

“Allocation method” means a method used to value land by estimating from sales of comparable improved properties a typical ratio of improved land to total value and applying that ratio to the improved property being analyzed to determine the value that the improved land contributes to the total value of the property.

8. Observe that NAC 361.118 3(c) specifies that if the subject property is improved land, the comparable properties must have a use that is consistent with that of the improved land. Strictly speaking, the assessor may not value improved land with vacant comparable sales. To get around this, the assessor could apply NAC 361.118 in reverse by adding the full cash value of improvements to land to estimate the value of the fully developed improved site. NAC 361.118 should really function as a two-way street that permits the assessor to value improved land with vacant sales or vacant land with improved sales by making market based full cash value adjustments to equalize the subject and comparables at the same stage of development.
9. Actually, NAC 361.118 as written merely attempts to value all improved land as vacant land, thereby making improvements to land intangible. When, contrary to NAC 361.118(c), an assessor uses vacant comparables to value improved sites, he must adjust the comparables upward for site development. In Nevada, as-if-vacant means selling price minus improvements on the land, not improved land valued as vacant land.
10. An exact definition of non-realty components with examples is needed to avoid confusion.
11. Modify the rules for tear-downs in NAC 361.118 2(b) by specifying a cutoff date (probably the sales cutoff date) for these things to occur. Also, the assessor should apply interim use adjustments to tear-downs that satisfy the time requirement and other conditions. This matches standard appraisal practice. Regulations for valuing interim use will be needed.
12. Clarify the rules for view adjustment. NAC 361.118 says that the county assessor shall make the view influence determination from any area on the parcel that is capable of development. Ordinarily, this includes any portion of the three dimensional envelope defined by the bundle of rights, like the roof of the house. This illustrates the need for a precise definition of land.
13. Clarify the term market conditions in NAC 361.118 or allow time adjustments specifically.
14. Clarify the meaning of the term “each area subject to the factor” in NRS 361.260 by adopting rules for conducting land factor studies. Because current law assigns no role to the Department in the land factor process, the Department also needs guidance from the Commission or Legislature to determine its specific duties.
15. NRS 361.333 (3) permits the department to use any statistical criteria that will indicate an accurate ratio of taxable value to assessed value and an accurate measure of equality in assessment. Does this latitude also apply to similar studies like land factoring?
16. How strictly do we interpret the Supreme Court’s direction that the “county assessors must use uniform standards and methodologies for assessing property values throughout the

state?” Does uniform mean identical? If so, to what extent must the Commission promulgate specific rules and procedures for valuation techniques like view influence and other market adjustments, land allocation and abstraction, land factoring, time adjustments, application of comparable sale analysis to mass appraisal using anything from base values to regression modeling, etc? Under a strict application, anything not explicitly codified in NRS or NAC would be unconstitutional.

17. The regulations cannot cover every situation, therefore, we should have a reference to national assessment administration standards from the IAAO, much like we already have a reference to Marshall Swift for a cost manual. Those standards are as follows:

- a.) Guide to Assessment Standards
- b.) Standard on Administration of Monitoring and Compliance Responsibilities
- c.) Standard on Assessment Appeal
- d.) Standard on Automated Valuation Models
- e.) Standard on Contracting for Assessment Services
- f.) Standard on Facilities, Computers, Equipment and Supplies
- g.) Standard on Manual Cadastral Maps
- h.) Standard on Mass Appraisal
- i.) Standard on Professional Development
- j.) Standard on the Valuation of Properties Affected by Environmental Contamination
- k.) Standard on Property Tax Policy
- l.) Standard on Public Relations
- m.) Standard on Ratio Studies
- n.) Standard on the Valuation of Personal Property
- o.) Standard on Digital Cadastral Mapping

Of these, the most important should be Mass Appraisal, Personal Property, and Ratio Studies. In the alternative, reference could be made to certain textbooks, such as “Property Appraisal and Assessment Administration (IAAO) or the 12th Ed. of the Appraisal Foundation’s “The Appraisal of Real Estate.”

19. Clarify the roles of NTC and SBE under NRS 361.333 and NRS 361.395.

20. Promulgate regulations on the use of the income approach. There are none, except in centrally-assessed.

21. Promulgate regulations on possessory interests. Drafts were considered by the Commission but were sent back for additional workshops. That process has not been completed.

22. Promulgate regulations on the valuation of off-the-shelf computer software. Drafts were considered by the Commission but were sent back for additional workshops. That process has not been completed.

23. Promulgate a regulation referencing all the mapping directions in the Assessment Manual that was never adopted (although its been around and used since the early 90's). Adopt the Manual of Assessment Policies and Procedures.
24. Promulgate enforcement regulations requiring compliance with reporting of sales to the Department in the form and manner required.
25. The State Board of Equalization should complete the regulatory process of reviewing county board regulations.
26. Promulgate standards for granting exemptions. For instance, does property owned by a hospital or other charity receive the exemption at the point when construction begins, or is mere ownership enough?

Exhibit 2 – List of Topics for Development of “Best Practices” Procedures

1. Land Valuation- detailed explanation of how values are determined
 - a.) Vacant
 - b.) Improved- what methods are used and a detailed explanation and example of how the appraisal is carried out.
2. NRS 361.4722 and 361.4723, Abatement of Property Tax
SEE ATTACHED EXAMPLE OF A PROPOSED QUESTIONNAIRE FORMAT FOR TOPICS
3. Sales Validation
 - a.) Copy of questionnaire sent to buyers and sellers submitted to department
 - b.) What other methods used
 - c.) Are all verified or is a sample taken
 - d.) If sampling, how is the sample selected
 - e.) How often are sales verified
 - f.) How are verified sales recorded
4. New Construction
 - a.) When is new construction picked up
 - b.) How is new construction discovered
 - c.) How often are sites under construction visited and at what stages
 - d.) How are interior improvements and builder options captured?
 - e.) Is a final inspection done when completed
 - f.) Are site measurements, building dept. and/or developer provided plans used
5. Marshall and Swift
 - a.) What adjustments are being used (foundation, seismic, wind, resort etc.)
 - b.) How do single unit in a multi unit building valued
 - c.) Are quality classes consistent with M & S descriptions
6. Subdivisions
 - a.) How are subdivisions qualified
 - b.) What paperwork do is required and where is it stored
 - c.) What is required to maintain subdivision status
7. Water Rights
 - a.) Are Water Rights obviously noted in files?
 - b.) Is there a tracking of recent sales?
 - c.) If rights are removed, did it affect the zoning & land use?
8. Agricultural property
 - a.) How is property eligible for agricultural designation qualified?
 - b.) Are agricultural applications taken and where are they stored
 - c.) Are field inspections done at time of applications and re-appraisal to verify it qualifies
9. Personal Property
 - a.) How is it reported (a list by owner, form created by assessor, supporting docs)
 - b.) Is a sample for field inspection done to verify correctness of reports
 - c.) Process for non-reporters
 - d.) How are leases processed

10. Files and File Contents

- a.) File for every parcel?
- b.) Contents in file
- c.) How are files stored and organized
- d.) How develop and keep up parcel maps and how often

11. Manufactured Homes (MH)

- a.) What is process when MH converts to real property
- b.) What method is used for valuing
- c.) Quality class issues

12. Training

- a.) Process for training new employees
- b.) What type of continued training is done
- c.) Any cross training

EXAMPLE FORMAT
Work Practices Evaluation Guide

Implementation of AB 489, SB 509

Topic List

Eligibility Claims

- Claim Forms
- Notification of Taxpayers
- Timeframe for acceptance

Classification of Property

- Existing Property
- New Property
- Residential Property
- Commercial or Other Property
- Mixed Use Property
- Rental Property

Computer Programming

Formula Calculation

Appeals

- Appeal Forms
- Communication with Treasurer
- Brochures on Appeal Rights

Application of Recapture

Determining tax rates exempt from abatement calculation

Redevelopment Districts

Annexation

Correction of Abatements

Application of multiple abatements

AB 489 imposes a system of calculating an abatement, or reduction, of tax liability. Two types of abatements were created, one for single family residences which are owner occupied and constitute the primary residence of the owner, as well as for certain qualifying rental properties. (NRS 361.4723).

The second type of abatement is applied to all other parcels or other taxable unit of property, including centrally-assessed property, with certain exceptions. (NRS 361.4722)

A county assessor shall receive claims for primary residential abatements and residential rental abatements and identify each parcel . . .for which such a claim is received. . .

Eligibility Claims

Refer to: LCB File No. R011-06, Sections 11 & 12.

NRS 361.4723 Claims	Yes	No	N/A or Other	Your Comments
Do you send eligibility claim forms to all home-owners annually?				
If you do not send claim forms to all home-owners annually, do you send eligibility claim forms to all new property owners?				
Does the claim form conform to the requirements of R011-06, Section 12?				Attach example.
When do you send claim forms?				
Do you have an audit program in place to verify the claims?				
How do you verify the home is owner-occupied? (a) check records; (b) rely on affidavit statement; (c) Other	(a)	(b)	(c)	
If you receive a claim after June 30, what procedures do you use?				
In applying NRS 361.773, what criteria do you use to determine "good cause"?				
Do you have brochures or information sheets available to taxpayers on how to claim the abatement?				
Do you have any automated reports on numbers of properties granted and/or denied eligibility?				
LCB File No. R011-06 Sec. 12 (2)(e) requires claimants to notify assessor if the property is no longer used as a SFR or is not the primary residence. Have you received any such notifications, and if so, approximately how many?				

Classification of Property

Refer to NRS 361.4722, NRS 361.4723

The owner of any parcel or other taxable unit of property . . . is entitled to a partial abatement . . . excluding any increase in the assessed valuation of the property . . .as a result of any improvement to or change in the actual or authorized use of the property

New Property	Yes	No	N/A or Other	Your Comments
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Is the value of an improvement which did not exist the previous year separately identified or segregated such that no abatement calculation is applied?				
When a final parcel map indicates a parcel is split from a larger property, is the cut parcel designated as new property?				
When a zoning change request by the taxpayer is granted, is the property designated as new property?				
When an apartment complex is converted to condominiums, is the property designated as new property?				
Describe how the automated system is used to designate new property, or provide an example.				
When boundary changes occur, are parcels on both sides of the boundary designated as new property? If no, please describe your procedure.				
What other indicators do you use to determine whether a change in the actual or authorized use has occurred?				
Is the difference between last year's value and this year's value called "new" or is the total value "new"?				
Was a substantial economic benefit created with a boundary line adjustment and therefore a New property?				
With a new house is the land also new? Or is the new house existing because the land was existing?				
How are parcels which were designated new in the prior year designated for application of the abatement in the current year?				
For property escaping taxation, how do you determine whether the property was subject to abatement in each year for which the property escaped taxation?				

Residential Property	Yes	No	N/A or Other	Your Comments
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Do you automatically grant the primary residence abatement to all buildings on a property which contains a SFR? If no, please describe the procedures you use to segregate property from the application of the primary residence abatement.				
Do you track home-business operations, to include a report of the numbers and types?				
Do you grant the primary residence abatement to property held in the name of a trust?				
Do you grant the primary residence abatement to property held in the name of an LLC, partnership, or other business entity? If yes, please provide examples.				
Describe any validation procedure you use to determine whether a claim for a primary residence has been made to any other county.				
Do you grant the primary residence abatement to multiple properties owned by the same family or family trust? Please explain.				

Refer to NRS 361.4724; LCB File No. R011-06, Section 14.

Rental Property	Yes	No	N/A or Other	Your Comments
Do you send eligibility claim forms to all multi-family residence properties annually?				
What discovery procedures are used to determine whether a claim form should be sent to the owner of a SFR?				
Do you require information regarding the nature and amount of utilities included in the rent? If yes, please describe.				
Do you calculate utility allowances in addition to the information provided by the Department?				
Is the procedure for determining whether the claimed rent exceeds HUD automated?				
Do you have an audit program in place to verify the claim? If yes, please describe.				
Do you grant the primary residence abatement for properties such as vacation homes? If so, describe the procedure for granting the abatement.				

Do you grant the 3% rental abatement to the entire property if less than all apartments meet the HUD income restrictions?				
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Personal Property	Yes	No	N/A or Other	Your Comments
Do you have any personal property accounts for which a <u>general</u> abatement has been granted? If yes, please describe the type of properties.				
When mobile home property is converted from personal property to real property, has a change in authorized or actual use occurred?				

Mixed Use Property	Yes	No	N/A or Other	Your Comments
If a portion of a SFR is rented, do you apply the primary residence abatement to the entire structure? If no, describe how you allocate the structure.				
If a portion of a primary residence parcel is used for another purpose, do you apply the primary residence abatement to the entire parcel? If no, describe how you allocate the parcel.				
If a mobile home eligible for the primary residence abatement sits on rented land, do you apply the primary residence abatement to the land?				
Can you have a converted mobile home on leased land?				

Remainder Property	Yes	No	N/A or Other	Your Comments
If a primary residence parcel is split, do you apply the 3% abatement to remainder parcels?				
Do you apply remainder based on percent of acres remaining or on percent of parcel value remaining?				