



ATTORNEYS AT LAW

Thomas M. Atherton

2700 First Indiana Plaza
135 North Pennsylvania Street
Indianapolis, IN 46204
Direct Dial: (317) 684-5348
Fax: (317) 223-0348
E-Mail: TAtherton@boselaw.com

January 24, 2008

Mr. Timothy Rushenberg
General Counsel
Department of Local Government Finance
Indiana Government Center North
100 North Senate Avenue, Room N1058
Indianapolis, IN 46204

Re: LaPorte County Ratio Studies

Dear Mr. Rushenberg:

On behalf of Mr. William Wendt, I submit the following response to the November 28, 2007 letter from the Nexus Group to Commissioner Musgrave (the "Nexus Letter").

The issue before the DLGF is whether the 2006 assessments in LaPorte County meet the standards of 50 IAC 21-1-1 *et seq.* The department has been presented with conflicting evidence in the form of LaPorte County's sales ratio study prepared by Nexus and the October 19, 2007 analysis of that study by Almy, Gludemans, Jacobs & Denne (the "Denne Report"). The November 28, 2007 Nexus Letter contained numerous factual and analytical errors and failed to substantiate the LaPorte sales ratio study. The first portion of this letter briefly summarizes the positions of Nexus and the Denne Report and clarifies the analytical differences between the LaPorte sales ratio study as outlined in the Nexus letter and the Denne Report. The second

portion of this letter presents information concerning “sales chasing” that invalidates the results of the LaPorte ratio study.

Looking past the irrelevancies and hyperbole that occupy much of the Nexus Letter, Mr. Kelly and Mr. Wuensch allege that the Denne Report contains three related errors. The first alleged error is that “...sales from 2004 and 2005 only should have been used to measure assessment quality.” Nexus Letter p. 5. The second alleged error is simply a corollary of the first, namely, that the Denne Report used too few of the 2004-2005 sales: “[a]gain, the sales database provided to Mr. Denne/Wendt and to the DLGF comprises about 2900 valid sales from the 2004-2005 time period. Mr. Denne’s October report uses only 472 of these valid sales.” Nexus Letter p. 6. The third alleged error is that “Denne implicitly invokes a new standard on Indiana assessment performance. He opines that one should take subsequent data outside the two years preceding the assessment date per 50 IAC 21 and utilize that data as the performance standard. In other words, 2006 sales data is the definitive test of the quality of 2006 assessment data.” Nexus Letter p. 6. Tellingly, Nexus does not say where Mr. Denne “opines” such a position. The alleged errors are discussed below.

The first and second alleged errors. These purported errors can be analyzed together as they are both premised on the same allegation: that there were thousands of valid 2004 and 2005 sales, hence it was error to look at the 2006 sales. Indeed, it seems curious at first glance that while the county identified thousands of purportedly valid 2004 and 2005 sales, the Denne Report used less than 500 of them. The answer is not, as Nexus suggests, that Mr. Denne’s analysis was based on “negligence of basic annual adjustment procedures as outlined in Indiana

Administrative Code.” Instead, the answer is that Mr. Denne understood and followed the IAAO Standards on ratio Studies which are incorporated by reference into the Indiana Administrative Code by 50 IAC 21-3-1, whereas Nexus did not. Contrary to Nexus’ assertion, under the IAAO Standards, there were not thousands of valid sales.

For background purposes, Standard 4.3 provides in pertinent part:

The basic physical characteristics of each property used in the ratio study must be the same when appraised for tax purposes and when sold or appraised by the review agency.... In the case of parcels with new improvements, for example, it is important to avoid matching sales prices of vacant lots against appraised values that include new construction, although such sales could be used in a ratio study for vacant land by using the appraised value of the land only. Besides new improvements, parcels should be checked for significant physical additions, renovations, or demolitions between the dates of assessment and sale. In general, parcels with such changes should be excluded from ratio studies. However, minor physical changes should not cause a parcel to be excluded. *Accord: 2007 Standards 3.4 and 4.1.4*

The Denne Report explains that one of its goals was “to ensure that the parcel as assessed was identical to the parcel as sold.” This mirrors the requirements of IAAO Standard 4.3. The reasons behind Standard 4.3 are straightforward. If, for example, a taxpayer bought a two bedroom house in 2004, but thereafter added a third bedroom assessable in 2006 pay 2007, it would be inappropriate to compare the 2004 sale price to the 2006 assessment because the 2004 sale would not provide meaningful information about the validity of the 2006 assessment.

The reason that so many 2004 and 2005 LaPorte sales were excluded from the Denne Report is because the properties’ physical condition – as reflected on LaPorte County’s own records – changed between the date of assessment and the date of sale.

The Denne Report explains that, “[t]he field for ‘significant changes’ in the sales files submitted to DLGF for these years could not be used for this purpose [to verify whether there had been significant physical changes between assessment and sale] inasmuch as all records had blanks in this field, as was also the case with the extra parcel identifier fields.” Denne Report p.

7. Since Nexus’ LaPorte data were insufficient,

Special measures were required, however, to ensure that the parcel as assessed was identical to the parcel as sold, which were as follows. A copy of the assessor’s database was obtained, which included both the current and all historical versions of the parcel records for over a decade. A special program was written to extract the dates and changes to each parcel’s recorded objective physical characteristics over that time period, and write them to a new file. That new file was then used to eliminate from further analyses any parcel that was sold in 2004 or 2005 but recorded as having had revised physical characteristics in the period between the time of sale and the time of assessment. *Id.*

In summary, it was impossible to tell from LaPorte’s submitted data whether the properties were physically the same when sold as when assessed. However, a detailed review of the assessor’s own records showed that most of the 2004 and 2005 sales submitted by LaPorte experienced changes in physical characteristics between the date of the assessment and the date of sale. Most of LaPorte’s data simply did not meet the requirements of IAAO Standard 4.3: “The basic physical characteristics of each property used in the ratio study **must** be the same when appraised for tax purposes and when sold.” (*Emphasis added*). As a result, contrary to the unsupported assertion by Nexus that there were thousands valid sales from 2004 and 2005, there were not. Faced with an inadequate data population, Mr. Denne then examined 2006 sales and trended them for time. This practice is specifically approved by both the IAAO Standards and 50 IAC 21-3-3 (c) (“If the sales data available is insufficient to satisfy the IAAO standard, the

local assessing official may use sales from earlier or more recent time periods, or both, by adjusting and time trending the sales data as described in the IAAO standard.” (emphasis added)).

The problems with physical changes to the sales are set out on page 7 of the Denne Report. The Nexus letter does not challenge Mr Denne’s findings that a review of the assessor’s records shows a multitude of changes in physical characteristics between the date of assessment and the date of sale. Nor does Nexus challenge the requirements of IAAO Standard 4.3. Instead, Nexus challenges Mr. Denne’s motives and knowledge. The factual basis of Denne’s criticism is unimpeached.¹

The third alleged error. The third allegation is that Mr. Denne has “invoke[d] a new standard on Indiana assessment performance [under which] 2006 sales data is the definitive test of the quality of 2006 assessment data.” Nexus Letter p. 6. It is probably sufficient to point out that the Denne Report never makes such a suggestion and no fair reading of the Denne Report could reach that conclusion. As pointed out above, Mr. Denne attempted to use 2004 and 2005 sales data, but too many of the sales had to be rejected because of property-specific changes reflected in the assessor’s records. In order to obtain a sufficient sample size, he augmented the valid 2004 and 2005 sales data with 2006 sales data. This is not the invocation of a new standard; it is application of the correct standard. See 50 IAC 21-3-3(c).

¹ Nexus’ only defense of the data is that since the DLGF marked the LaPorte data as “compliant,” “obviously all required fields were included for every valid sale.” The fact that the DLGF may have initially accepted LaPorte’s misrepresentations about the quality of its data cannot now be used as a defense to shield from review the errors in such data as revealed by the Denne Report.

Putting aside Nexus' unfounded assertions regarding the appropriate "standard," the Nexus Letter admits that the results obtained by evaluating the 2006 sales reveals errors in the LaPorte assessments. Nexus admits: "*Denne's October report, even though comprised mostly of sales from the 2006 time period, is vastly similar to our own preliminary analysis of LaPorte County (not contained herein).*" (Nexus Letter P. 10 Underscore added, italics in original.) The "vastly similar" Nexus studies using 2006 sales indicate that "many property classes in LaPorte County require further stratification, delineation, and re-examination" for 2007. Yet the plain facts are that the data errors that underlie the acknowledged poor results are not amenable to remediation by any process of stratification and trending, and that Indiana law specifically requires a reassessment in instances, such as here, where the coefficients of dispersion are unacceptable. 50 IAC 21-11-1. The effort of the county and Nexus to conceal such errors in light of their own "vastly similar" studies using 2006 sales is inequitable and contrary to Indiana law. One cannot cure the problems and errors in the piecemeal fashion Nexus proposes.

Qualifications of the Analysts. Pages 11 and 12 of the Nexus letter contain a largely self-congratulatory section entitled "**Qualifications of the Analysts.**" Ultimately, it is the quality of the data and analysis that is important rather than qualifications of the analyst. However, because Nexus devotes so much of their response to *ad hominem* attacks on Mr. Denne, I wanted to provide some unbiased sources in evaluating Mr. Denne's knowledge and qualifications. Mr. Denne is one of the IAAO members specifically acknowledged in the IAAO's text, *ASSESSMENT ADMINISTRATION*, International Association of Assessing Officers, 2003. Mr. Denne, along with other members of the IAAO Technical Standards Committee, is acknowledged with "special

thanks” in the 2007 Edition of the IAAO’s Standard on Ratio Studies. Moreover, Mr. Denne has been a pivotal player in the development and adoption of the IAAO Standards from their very inception.

The August 2007 edition of the IAAO’s magazine, *FAIR AND EQUITABLE*, focused on sales ratio studies. In the cover article entitled “The Journey to Revise the IAAO Standard on Ratio Studies,” Peter Davis, who chaired the IAAO’s Technical Standards Committee, wrote:

[I]n 1976, IAAO teamed up with the Lincoln Institute of Land Policy to sponsor a symposium on “Analyzing Assessment Equity.” A by-product of that meeting was the publication of the proceedings, which brought the association another step closer to an industry standard on ratio studies. Several participants at that conference are still very active members of IAAO today. Richard Almy was Director of the Research and Technical Services Department, Robert (Bob) Gloudemans held the title of Research Associate, and Robert Denne served as Research Associate and Librarian for IAAO. These three individuals played critical roles in the promotion and development of the first ratio study standard. They also have participated in every revision to the standard since then, including this most recent one. During the late 1970s, Almy, Gloudemans, and Denne, along with Stuart Miller, authorized a comprehensive reference manual for IAAO, titled *Improving Real Property Assessment* (IAAO 1978). That text was the first to devote a chapter to assessment ratio studies and measurements of assessment performance. (Emphasis added).

In a side bar to the article, “The Journey to Revise the IAAO Standard on Ratio Studies,” the members of the technical advisory committee are identified and Mr Denne is described as follows:

Robert Denne is another well-respected consultant with Almy, Gloudemans, Jacobs, & Denne. Robert joined the ad hoc Ratio Study Technical Advisory Subcommittee in 2006. He has a diverse background in ratio studies and mass appraisal and has been an important contributor to IAAO for more than 30 years.

I was unable to find any reference to Dr. Kelly, Mr. Wuensch, or Nexus in any of these publications.

Summary -- Part 1 Ultimately, the DLGF will have to evaluate the strengths and weaknesses of the information it has received in light of the *facts* on which each submission is based. Mr. Denne has submitted report(s) based on the data supplied by LaPorte County itself, and he has evaluated the LaPorte County data and sales ratio study pursuant to the IAAO Standards that are incorporated into Indiana law. By contrast, the Nexus response is comprised largely of unfounded *ad hominem* attacks and unsupported assertions regarding the requirements of Indiana law. Most importantly, the IAAO Standard requires that, “the basic physical characteristics of each property used in the ratio study must be the same when appraised for tax purposes and when sold.” The LaPorte ratio study does not satisfy this mandate and, therefore, is not a valid study under 50 IAC 21-3-1.

Part Two - Sales Chasing

50 IAC 21-3-1 provides, “[l]ocal assessing officials shall perform all ratio studies using the methods or combination of methods acceptable under the [1999] Standard on Ratio Studies published by the International Association of Assessing Officers (IAAO standard) or other acceptable appraisal methods approved by the department.” As will be shown below, sales ratio studies that involve sales chasing do not comply with the IAAO Standard and consequently do not meet the requirements of 50 IAC 21-3-1.

Section 15 of the Standard describes sales chasing as follows.

Sales chasing is the practice of using the sale of a property to trigger a reappraisal of that property at or near the selling price. Sales chasing causes invalid uniformity results in a sales ratio study and causes invalid appraisal level results unless similar unsold parcels are reappraised by a method that produces an appraisal level for unsold properties equal to the appraisal level of sold properties.

Thus, if a ratio study involves sales chasing, the both the uniformity and appraisal level results are “invalid” unless the unsold parcels are reappraised.

Section 10 of the IAAO Standard expounds on why sales chasing can invalidate ratio studies:

The objective of a ratio study is to determine appraisal performance for the population of properties. As long as sold and unsold parcels are appraised in the same manner, statistics calculated in a sales ratio study can be used to infer appraisal performance for unsold parcels. However, if parcels that sell are selectively reappraised based on their sales prices or some other criterion (such as listing price), sales ratio study uniformity measures will not be valid (appraisals will appear more uniform than they are). In this situation, measures of appraisal level will also be invalid unless similar unsold parcels were reappraised by a method that produces the same percentage of market value (appraisal level) as on the parcels that sold. Assessing officials must ensure that sold and unsold parcels are treated equally. Several techniques are available for determining whether assessors are selectively appraising sold parcels (see IAAO [1990, appendix 20-2] and Gloudemans [1999, chapter 6]) for a more detailed discussion).

If unsold properties are not appraised consistently with sold properties and applicable guidelines, unadjusted sales ratio results cannot be used. The oversight agency will have to adjust calculated results or conduct an alternative study (see section 10.7). In addition, the appraisal agency should be ordered to cease the unprofessional practice of sales chasing and to reappraise all property on a consistent basis using applicable standards and guidelines. (Emphasis added.)

Since an apparently valid ratio study could in fact be invalid if it involved sales chasing, I asked Mr. Denne to analyze the LaPorte sales ratio study to determine whether the data indicate sales chasing. The statistical analysis of LaPorte’s ratio study reveals that there is a greater than

99% level of confidence that sales chasing occurred. A copy of that analysis is attached as Exhibit A.

A few explanatory comments may be in order. Table 1 examines the LaPorte data in three ways: (a) with all the data; (b) with the extremes trimmed; and (c) with outliers trimmed. Mr. Denne presents all three “in order to help establish the sensitivity of the test,” but suggests that method (a) is the best way to analyze the data. The most important point, however, is that (a), (b), and (c) all indicate with a degree of confidence in excess of 99% that the LaPorte study involved sales chasing. To paraphrase the IAAO Standard, “since unsold properties [were] not appraised consistently with sold properties and applicable guidelines, [the] unadjusted sales ratio results cannot be used.”

Table 2 provides confirming evidence. It examines the extent to which adjustments were made to subjective factors such as grade in the sold and unsold properties. Again the p-value² demonstrates that for the county as a whole and for 13 townships, one can be 99% confident that the subjective factors were handled differently for sold and unsold properties. In an additional 3 townships, one can be 95% certain that subjective factors were handled differently for sold and unsold properties.

Summary – Part II. One can be confident to a 99% degree of certainty that sold and unsold properties were treated differently by the LaPorte assessing officials. This practice makes the LaPorte study in violation of the both the standards and 50 IAC 21-3-1. Ultimately, La Porte

² The p-values in Table 1 are computed using the Mann-Whitney test, while the p-values in Table 2 were computed using the chi square test, which is more appropriate since Table 2 involves “count data.” Both tests are standard statistical analyses referred to in the Standard, and both results are interpreted the same; that is, the lower the indicated value, the more unlikely it is that the differences are caused by chance.

Mr. Timothy Rushenberg
January 24, 2008
Page 11

County has not provided a valid or persuasive ratio study. The only ratio study that meets the Standard and 50 IAC 21-3-1 is the one provided by Mr. Denne. That study demonstrates multiple failures in LaPorte County assessing performance that under the terms of 50 IAC 21-11-1 require a reassessment.

Very truly yours,

Thomas M. Atherton

TMA:
Enclosure