



Washington State Auditor's Office

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Whistleblower Investigation Report Department of Revenue

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March 10, 2016

Vikki Smith, Director
Department of Revenue

Report on Whistleblower Investigation

Attached is the official report on Whistleblower Case No. 15-029 at the Department of Revenue.

The State Auditor's Office received an assertion of improper governmental activity at the Agency. This assertion was submitted to us under the provisions of Chapter 42.40 of the Revised Code of Washington, the Whistleblower Act. We have investigated the assertion independently and objectively through interviews and by reviewing relevant documents. This report contains the result of our investigation.

Questions about this report should be directed to Whistleblower Manager Jim Brownell at (360) 725-5352.

Sincerely,

A handwritten signature in cursive script that reads "Troy X. Kelley".

TROY KELLEY
STATE AUDITOR
OLYMPIA, WA

cc: Governor Jay Inslee

Karin Hendrickson, Internal Audit Manager

Kate Reynolds, Executive Director, Executive Ethics Board

Jennifer Wirawan, Investigator

WHISTLEBLOWER INVESTIGATION REPORT

Assertions and results

Our Office received a whistleblower complaint asserting three Department of Revenue (Department) managers engaged in the following improper governmental actions:

Assertion 1:

Three Department managers held private meetings with companies to discuss value assessments instead of using the formal hearing process, which violates state law and rules.

We found no reasonable cause to believe an improper governmental action occurred.

Assertion 2:

Three Department managers instructed Department appraisers to use predetermined value assessments in violation of state law and the Uniform Standards of Professional Appraisal Practice.

We found no reasonable cause to believe an improper governmental action occurred.

Background

Annually the Department assesses a true and fair market value for each intercounty or interstate utility operating in the state. The utility companies include gas, telephone, railroad, airline, cellular and electric companies. The state taxable value of each company's operating property ranges from \$10,000 to \$4 billion.

At the beginning of the calendar year Department appraisers send out annual reporting forms to each company. The companies are required by law to complete the 50-page form and return it to the Department by March 15. A company may request up to two 30-day extensions. Department appraisers use generally accepted appraisal practices and a standardized template to determine taxable value. For each assessment, the appraiser develops a value range using various methods such as cost, income, and market approaches. The appraiser selects their opinion of fair market value from within this range.

State law (RCW 84.12.270) requires the Department to assess the true and fair value, the appraiser's opinion of value, of all the operating property for each company by June 30. According to a Property Tax Division manager, a supervisor generally conducts quality control reviews of appraisals.

By July 1 letters are sent to the companies with the assessed value and information regarding the company's right to request a hearing.

The Department has established a rule (WAC 458-50-070(4)) that requires the final assessed value of each company be made on or before August 20. If a company wishes to appeal the assessed value, it can do so through the Board of Tax Appeals or superior court.

About the Investigation

We interviewed witnesses, examined documentation, reviewed email communications and spoke with the three subjects (Subject 1, Subject 2, and Subject 3).

Meetings

We found there were no hearings held in calendar year 2014; all value disagreements were resolved through an informal meeting process. The meetings were described by witnesses and the subjects as discussions between the company and the appraiser, and in some cases the appraiser's supervisor. The meetings may consist of multiple conversations, either in person or by telephone, between the appraiser and the company representative.

Witnesses said the meetings began approximately six or seven years ago as a means to resolve minor or technical issues with value assessments. For instance, instead of going through the hearing process to report a misplaced number, the company could simply call the appraiser and resolve the matter informally. As time went on, companies requested the meetings at an increasing rate.

The subjects described the formal hearing process as one-sided and said the meetings are more beneficial to both the state and the companies. Subject 2 said the meetings "are discussions, which are more open and taxpayer sensitive." Subject 1 said there is "no way" she would "close the door on the data" by refusing to listen to a company outside of a hearing.

Nothing in state law precludes agencies from having discussions with taxpayers. Therefore, we found no reasonable cause to believe an improper governmental action occurred.

Value Assessments

We examined the Department's appraisal files for the 13 companies that received the highest value reductions in 2014. Documentation was sparse regarding what was discussed during the meetings, or the appraiser's justification for reduction of taxable value. However, each appraiser was able to explain their thought processes and opinions, which ultimately resulted in the reductions in value.

We interviewed witnesses who said they often felt pressured and stressed about the process of meeting with taxpayers. As a result, they said some appraisers have intentionally inflated the tentative values of companies so when the value is reduced the company can feel as if it got a "win." One witness said this process is "unfair to companies who don't request an appeal."

When asked about the process, the subjects said they are not aware of any appraisers intentionally inflating their opinion of tentative value. However, Subject 1 said, “It is not uncommon for an appraiser to pick a higher number so there is a little bit of space for negotiation in the case of an appeal.” However, she expects the appraiser to pick a “reasonable value” and cannot picture any of them picking an unreasonable value. When asked what occurs if the company does not request a hearing, she said the appraiser should “put it back where it’s supposed to be.” Subject 2 said part of the appraiser’s job is to manage the relationship with the company and if that is the way the staff person manages the company he is “ok with it” as long as they are within a supportable value range. Subject 3 said there are a “variety of strategies” used by Department appraisers and “some are more exact than others.”

Although witnesses said some appraisals had inflated tentative values, we found no evidence the subjects directed this practice. Therefore, we found no reasonable cause to believe the subjects engaged in an improper governmental action.

State Auditor’s Office Concluding Remarks

We thank Agency officials and personnel for their assistance and cooperation during the investigation.

WHISTLEBLOWER INVESTIGATION CRITERIA

We came to our determination in this investigation by evaluating the facts against the criteria below:

Assertion 1:

RCW 84.12.340 Hearings on assessment, time and place of.

Following the making of an assessment, every company may present a motion for a hearing on the assessment with the department of revenue within the first ten working days of July. The hearing on this motion shall be held within ten working days following the hearing request period. During this hearing, the company may present evidence relating to the value of its operating property and to the value of other taxable property in the counties in which its operating property is situate. Upon request in writing for such hearing, the department shall appoint a time and place therefor, within the period aforesaid, the hearing to be conducted in such manner as the department shall direct. Hearings provided for in this section may be held at such times and in such places throughout the state as the department may deem proper or necessary, may be adjourned from time to time and from place to place and may be conducted by the department of revenue or by such member or members thereof as may be duly delegated to act for it. Testimony taken at this hearing shall be recorded.

WAC 458-50-070 Annual assessment – Procedure.

(3) Hearings.

(a) In general. Each company may petition the department for a hearing relating to the value of its operating property as tentatively determined by the department and to the value of other taxable properties in the counties in which its operating property is situated. Such petition shall be made in writing and filed with the department within the first ten working days of July. The department shall appoint a time within ten working days following the hearing request time period for the conduct of such hearing, which may be held in such places throughout the state as the department may deem proper or necessary. Notice of the time and place of any or all hearings shall be given to any person upon request.

(b) The hearing shall be conducted by the director or by any employee or agent of the department designated by the director. A record of the proceedings shall be kept and shall be considered a public record. The hearing shall be recorded with a recording device and the recordings shall become a part of the record of the proceedings and considered a part of the public record. All records and documents presented at the hearing shall become a part of the record of the proceeding and shall be considered a part of the public record, except as provided in (c) of this subsection.

(c) The hearing shall be open to the public, except (i) when the company proposes to offer in evidence information relating to its assessment if disclosure of such information to other persons would violate the company's right to privacy or would result in an unfair competitive disadvantage to such company; or (ii) when the department proposes to offer in evidence information which has been obtained pursuant to RCW 84.12.240 if the disclosure of such information to other persons would violate the company's right to privacy or would result in an unfair competitive disadvantage to such company. The hearing at this point shall be closed to the public unless the company consents to the proceeding remaining open to the public.

(d) Testimony recorded, and all records and documents of a confidential nature introduced, during the period when the hearing is closed to the public shall become a part of the record, but shall not be disclosed except upon order of a court of competent jurisdiction or upon consent of the company.

(e) Records of the proceedings shall be maintained for a period of seven years following the close of the hearing.

(4) Determination of final value. On or before the twentieth day of August, the department shall make a final determination of the true and correct actual cash value of each company's operating property appearing on the assessment roll. The department may raise or lower the value from that amount tentatively set pursuant to this section: Provided, That failure of a company to request a hearing shall not preclude the department from setting a final value higher or lower than that amount tentatively set pursuant to this section: Provided further, That where a company has not requested a hearing, the department shall not adopt a

final value higher than that tentatively set except after giving five days written notice to the company. The department shall notify each company by mail of the final true and correct actual cash value as determined by the department.

Assertion 2:

RCW 84.12.270 Annual assessment – Sources of information.

The department of revenue shall annually make an assessment of the operating property of all companies; and between the fifteenth day of March and the first day of July of each year shall prepare an assessment roll upon which it shall enter and assess the true and fair value of all the operating property of each of such companies as of the first day of January of the year in which the assessment is made. For the purpose of determining the true and fair value of such property the department of revenue may inspect the property belonging to said companies and may take into consideration any information or knowledge obtained by it from such examination and inspection of such property, or of the books, records, and accounts of such companies, the statements filed as required by this chapter, the reports, statements, or returns of such companies filed in the office of any board, office, or commission of this state or any county thereof, the earnings and earning power of such companies, the franchises owned or used by such companies, the true and fair valuation of any and all property of such companies, whether operating or nonoperating property, and whether situated within or outside the state, and any other facts, evidence, or information that may be obtainable bearing upon the value of the operating property: PROVIDED, That in no event shall any statement or report required from any company by this chapter be conclusive upon the department of revenue in determining the amount, character, and true and fair value of the operating property of such company.

WAC 458-50-080 True cash value – Criteria.

(1) The true cash value of the operating property of public utilities is its "market value," i.e., the amount of money a buyer willing but not obligated to buy would pay for such operating property from a seller willing but not obligated to sell. In arriving at a determination of such value the department may consider only those factors which can within reason be said to affect the price in negotiations between a willing purchaser and a willing seller, and the department shall consider all such

factors to the extent that reliable information is available to support a judgment as to the probable effect of such factors on price.

WAC 458-50-170 Valuation principles.

What is meant by "true and fair value"? One hundred percent of true and fair value is the standard used by assessing officials for valuing both taxable property and exempt property. True and fair value is the same as market value or fair market value. It is the amount of money a buyer of property willing but not obligated to buy would pay a seller of property willing but not obligated to sell, taking into consideration all uses to which the property is adapted and might in reason be applied. This term incorporates all the rights and benefits, present and future, associated with the ownership of property.

WAC 458-10-060 Standards of practice.

The standards of practice adopted by the department and governing real property appraisal activities by accredited appraisers are the generally accepted appraisal standards as evidenced by the current appraisal standards promulgated by the Appraisal Standards Board of the Appraisal Foundation. A complete text of these appraisal standards is available for viewing during normal working hours at the property tax division of the department.

Uniform Standards of Professional Appraisal Practice (USPAP) 2014-2015 Edition

Definitions

APPRAISAL: (noun) the act or process of developing an opinion of value; an opinion of value.

Ethics Rule

Conduct: (U-7 lines 228-235)

An appraiser must perform assignments with impartiality, objectivity, and independence, and without accommodation of personal interests.

An appraiser:

- Must not perform an assignment with bias;
- Must not advocate the cause or interest of any party or issue;
- Must not accept an assignment that includes the reporting of predetermined opinions and conclusions;

Management: (U-8 lines 274-280)

An appraiser must not accept an assignment, or have a compensation arrangement for an assignment, that is contingent on any of the following:

1. The reporting of a predetermined result (e.g., opinion of value);
2. A direction in assignment results that favors the cause of the client;
3. The amount of a value opinion;
4. The attainment of a stipulated result (e.g., that the loan closes, or taxes are reduced);