POLICY
brief
Washington Research Council
PB 07-03 February 12, 2007

Property Tax Bills Before the 2007 Legislature

BRIEFLY

The legislature is again considering measures to provide property tax relief to homeowners. Funding such relief by shifting the burden onto business would hurt the competitiveness of the state's economy.

The recent hot real estate market has sent assessed values soaring. While legal caps on property tax revenue growth have brought reductions in tax rates that largely offset the rising assessments, certain property owners—those whose properties have gone up in value much more than average—have seen substantial tax hikes, and many other property owners fear (erroneously) that higher taxes will inevitably follow from their higher assessments. In reaction, legislators have introduced a number of bills this session to offer targeted tax relief for homeowners.

When homeowner relief takes the form of new or expanded exemptions for residential property, however, the end result is higher property taxes for business. The overall level of business taxation is greater in Washington than in most other states. Property tax reforms that exacerbate this problem are ultimately a bad deal for all Washington taxpayers.

Washington's Property Tax

Washington's reliance on the property tax dates back to the establishment of Washington Territory in 1853. In the early years of statehood the property tax was the principle source of state and local revenue. Today, property taxes remain the largest source of revenue for local governments in Washington. There are 1,700 separate taxing jurisdictions levying a property tax in Washington, ranging from the state government itself to library, fire, school, and mosquito districts. All together they collected $6.9 billion in property tax revenue in 2005. Property taxes provide 12 percent of state General Fund revenue and 43 percent of local government tax revenue.

The property tax remains unpopular with Washington's taxpayers. Belying this unpopularity, the property tax burden in Washington is about average compared to other states, equal to $1,029 per capita in 2004 (ranking 22nd among the states) or 2.9 percent of state personal income (ranking 29th). Some would even say that Washington's property taxes are remarkably low given the state has no income tax. Taxpayers are protected by the state constitution's strong requirement for uniformity, as well as by laws that limit local governments' ability to increase tax levies without explicit permission from their voters.

Washington Research Council
108 S Washington St., Suite 406
Seattle WA 98104-3408
voice: 206-467-7088
fax: 206-467-6957
www.researchcouncil.org

State and Local Property Taxes in 2004

Per Capita

		Rank
New Jersey	$2,099	1
Connecticut	$1,944	2
New Hampshire	$1,940	3
New York	$1,677	4
Rhode Island	$1,629	5
Maine	$1,597	6
Massachusetts	$1,532	7
Vermont	$1,531	8
Illinois	$1,407	9
Wyoming	$1,352	10
Wisconsin	$1,350	11
Alaska	$1,306	12
Texas	$1,254	13
Kansas	$1,188	14
Michigan	$1,186	15
Nebraska	$1,148	16
Maryland	$1,082	17
Iowa	$1,080	18
Florida	$1,064	19
Montana	$1,034	20
Virginia	$1,031	21
Washington	$1,029	22
Colorado	$1,026	23
Pennsylvania	$1,010	24
Ohio	$981	25
Indiana	$975	26
Minnesota	$965	27
California	$963	28
Oregon	$963	28
Nevada	$920	30
North Dakota	$919	31
South Dakota	$915	32
South Carolina	$882	33
Georgia	$880	34
Arizona	$848	35
Idaho	$777	36
Missouri	$747	37
North Carolina	$713	38
Utah	$689	39
Mississippi	$641	40
Tennessee	$608	41
Hawaii	$571	42
Delaware	$546	43
West Virginia	$540	44
Kentucky	$516	45
Louisiana	$502	46
Oklahoma	$465	47
New Mexico	$441	48
Arkansas	$400	49
Alabama	$367	50
United States	$1,084	
District of Columbia	$1,856	

Source: Urban Institute-Brookings Tax Policy Center/Census Bureau

Uniformity

As explained in our report "Preserve Property Tax Uniformity to Maintain Washington's Economic Competitiveness" (WRC 2000) most tax authorities believe that uniformity is the foundation of good property tax systems. A uniform property tax embodies the fundamental notion of fairness: All property owners are treated equally. In addition, a uniform system is economically neutral, not favoring one form of property over another. Looking across the nation, most departures from uniformity result in shifts of tax burden onto businesses and away from households, reducing the attractiveness of the state to property-intensive businesses.

Article VII, section 1 of the original state constitution included a very strong uniformity requirement, "The legislature shall provide by law a uniform and equal rate of assessment and taxation on all property in the state." This has since been modified to read, "All taxes shall be uniform upon the same class of property within the territorial limits of the authority levying the tax… All real estate shall constitute one class…. Such property as the legislature may by general laws provide shall be exempt from taxation." The legislature has used the flexibility so granted to exempt many forms of personal property, including household goods and personal effects; intangible personal property such as stocks, bonds and bank accounts; motor vehicles; and business inventories. Today only personal property used in business (mainly machinery) is subject to the property tax. The Washington property tax has become mainly a tax on real estate. For this class of property the uniformity requirement still applies, with limited exceptions.

Article VII, section 10 allows the legislature to grant exemptions (means-tested or otherwise) to retired persons. Under this provision the legislature has established three means-tested exemptions. First, seniors (age 61 and older), non-senior disabled retirees and disabled veterans are exempt from excess levies on a portion of the assessed value of their home if their incomes are below $35,000. Second, for some individuals, the assessed value of the primary residence is frozen at the level of either 1995 or the year the individual reached 61 or became disabled, if later. Third, seniors, disabled retirees and disabled veterans are exempt from regular levies if their incomes are below $30,000.

In addition, homeowners above the age of 59 with an income of less than $40,000 are eligible to defer payment of taxes until the house is sold.

One percent rate cap

Article VII, section 2 of the constitution limits the aggregate property tax that can be levied on a particular property to 1 percent of the value of the property ($10 per $1,000) unless otherwise approved by the voters. Levies under the 1 percent limit are termed "regular" levies. Levies in excess of this amount are "excess" or "special" levies.

State and Local Property Taxes in 2004

Per $1,000 of State Personal Income

			Rank
Maine	$	53.10	1
New Hampshire	$	53.00	2
New Jersey	$	50.40	3
Vermont	$	48.10	4
Rhode Island	$	47.60	5
New York	$	43.80	6
Connecticut	$	42.90	7
Wisconsin	$	42.00	8
Texas	$	40.80	9
Illinois	$	40.50	10
Wyoming	$	39.40	11
Alaska	$	38.40	12
Kansas	$	38.20	13
Montana	$	37.40	14
Michigan	$	37.00	15
Massachusetts	$	36.30	16
Nebraska	$	35.50	17
Iowa	$	34.80	18
Florida	$	33.80	19
South Carolina	$	32.50	20
Indiana	$	32.30	21
Ohio	$	31.50	22
Oregon	$	31.50	22
North Dakota	$	31.10	24
Pennsylvania	$	30.30	25
South Dakota	$	30.30	25
Arizona	$	29.60	27
Georgia	$	29.50	28
Washington	$	29.40	29
Idaho	$	28.90	30
Virginia	$	28.50	31
Colorado	$	28.40	32
California	$	27.30	33
Maryland	$	27.30	33
Nevada	$	27.20	35
Minnesota	$	26.70	36
Mississippi	$	26.10	37
Utah	$	25.90	38
Missouri	$	24.50	39
North Carolina	$	24.30	40
West Virginia	$	20.90	41
Tennessee	$	20.40	42
Kentucky	$	18.90	43
Louisiana	$	18.40	44
Hawaii	$	17.50	45
New Mexico	$	16.90	46
Oklahoma	$	16.70	47
Arkansas	$	15.50	48
Delaware	$	15.30	49
Alabama	$	13.30	50
United States	$	32.80	
District of Columbia	$	36.30	

Source: Urban Institute-Brookings Tax Policy Center/Census Bureau

Regular levies are implemented through a complex web of state statutes. Of the $10 per $1000, $3.60 is reserved for the state government. Various local governments divide $5.90 (counties get $1.80; cities get up to $3.60; county road districts get $2.25; and so forth). The remaining $0.50 is reserved for open space preservation, emergency medical services, and affordable housing.

Special levies must be voter approved. They are generally approved for one year but may last for two to six years for school and fire districts. Levies dedicated to paying interest and principle on voter-approved bonds may extend even longer.

Caps on annual revenue growth

In 1971 the legislature imposed a cap on the annual increases in local government regular property tax revenues. This cap (the 106 percent limit) limited the amount a local government can collect from its regular property taxes in any year to 106 percent of the highest amount of revenue received from its regular levy in the preceding three years, plus an increment representing the existing tax rate applied to the value of new construction.

This limit is placed on the aggregate amount that can be collected in a year and not on the amount collected from an individual property. Under the limit, therefore, different property owners can experience different rates of tax increase. A homeowner whose property goes up in value relative to other properties in the area will see a greater than average tax increase; vise versa, a property owner whose property increases in value less than others in the district will see a smaller than average tax increase.

Since this limit was enacted in 1971 there have been several attempts to further limit annual tax increases. In 1979 the legislature extended the 106 limit to the state property tax. In 1997 voter-approved Referendum 47 further limited annual increases in state revenues to the lesser of 6 percent or inflation. For local governments, Referendum 47 required evidence of “substantial need” to be presented before revenues could be raised by more than the inflation rate.

In 2001 voters passed Initiative 747, which restricted regular property tax increases for the state and other districts to the lesser of inflation or one percent. Like the 106 percent limit, this limit applies to the aggregate amount that can be collected annually. However, a state superior court last year ruled I-747 unconstitutional on a technicality. This ruling is currently under appeal to the state Supreme Court.

PENDING LEGISLATION

As of February 8, legislators had introduced 48 pieces of legislation regarding the property tax. We discuss below a number of the more significant pieces, including three proposals that would weaken the constitutional uniformity protection.

Constitutional amendments

Three constitutional amendments have been proposed this session that would further empower the legislature to limit certain taxpayers' property tax liabilities.

HJR 4205. Modeled after California's Proposition 13, House Joint Resolution (HJR) 4205 would limit the annual increase in a property's assessed value for the state property tax to one percent. When its ownership is sold or transferred a property would be reassessed to100 percent of fair market value. Its assessed value would then again be limited to increasing at 1 percent a year for tax purposes.

As the amendment would do nothing to restrain the growth of the overall state property tax revenue, this assessment system would shift the property tax burden towards those properties experiencing less than average rates of appreciation as well as those which have recently changed hands.

California's experience with Prop. 13 has been mixed (O'Sullivan, Sexton and Sheffrin 1995). Homeowners whose homes have greatly increased in value have benefited the most from the 1 percent cap. The cap also raises questions of fairness. Two people in identical homes, next-door to each other can pay substantially different property taxes. It also provides a disincentive to sell property, causing people to stay in a home sometimes much longer than they otherwise would to avoid paying the higher tax rate.

SJR 8210. This constitutional amendment would allow the legislature to exempt the first $50,000 dollars of valuation on a primary residence from property taxation. This homestead exemption would represent a significant departure from uniformity and would shift property tax burden on to businesses.

The related bill *SB 5187* would implement the homestead exemption. The exemption established by SB 5187 would only apply to the state property tax. However, nothing would preclude the legislature from extending the exemption to local taxes in the future.

State analysts estimate that SB 5187 would result in no revenue loss to the state, as the loss in tax base from the homestead exemption would be fully offset by an increase in the state property tax rate. Fifty-six million dollars in property taxes would be shifted from homeowners to other taxpayers in 2008 as a result of the exemption, with the number growing to $107 million in 2009.

SJR 8218. As we noted above**,** article VII, section 10 of the state constitution authorizes the legislature to grant exemptions to retired persons. This amendment adds to that section the sentence "Additionally, relief on the assessed valuation of real property may be granted to property owners based solely on condition of age without respect to income." It is unclear that the current language of the constitution prohibits such a cap, however.

The related bill *SB 5707* would implement a valuation growth cap. For homeowners 61 years of age or older, the annual increase in assessed value would be capped at 5 percent. This cap would shift property taxes away from senior homeowners onto other homeowners and businesses. The greatest benefits would accrue to those experiencing the greatest rates of appreciation on their homes.

Bills to expand existing breaks for seniors, the disabled and veterans

A number of bills would expand the existing exemptions for seniors, disabled retirees and disabled veterans.

HB 1578. This bill would allow senior citizens to deduct Medicare premiums, ocular devices, and hearing instruments from their disposable income, which will allow more seniors to qualify for the property tax exemptions by lowering their calculated disposable income. Other legislation proposed would allow the deduction of disability benefits as well.

HB 1596 and SB 5201. The maximum income for retired persons to be eligible for exemption is currently capped at $35,000 for excess levies and $30,000 for regular levies. These bills have been proposed to increase the maximum income under which seniors can qualify for property tax exemption on all or a portion of their house's value. Under this proposal the income cap for exemptions would be increased to $40,000 for excess levies and $35,000 for regular levies. These would be the income thresholds for 2008 and in subsequent years the maximum income levels and the exemption amounts would be tied to inflation.

HB1629. This bill raises the income threshold even further to $50,000 for excess levies and $45,000 for regular levies. It would also tie the income levels and exemption amounts to inflation.

SB 5737. This bill would extend the existing means-tested valuation freeze for seniors, disabled retirees and disabled veterans to all seniors, disabled retirees, and disabled veterans.

In general, the freeze shifts property taxes away from the targeted homeowners and on to other homeowners and businesses. The greatest tax savings accrue to those whose homes have appreciated the most.

While state analysts estimate that the bill will result in no loss in state property tax revenue, those local governments with very low rates of property appreciation will lose revenue. The impact builds over time. By 2013, local government revenue loss is forecast to be $27.0 million. By that year the amount of state and local taxes shifted onto other property owners is forecast to be $280.7 million.

Bills to expand breaks for veterans

Several bills focus narrowly on disabled veterans.

HR 1102. This bill was introduced in the House to increase the income threshold under which veterans who are retired due to service related disabilities can claim an exemption from all or a portion of the property tax. Under this bill, retired veterans with an income of less than $70,000 would be exempt from all excess levies and regular property taxes levied on the greater of $60,000 or 60 percent of the valuation of the home.

The Department of Revenue estimates that losses to local governments from this exemption will be $149,000 in 2008. In addition $271,000 in state school levy revenues will be shifted to other taxpayers in 2008, rising to $874,000 for the 2007-2009 biennium. A total of $1.1 million in property tax revenues will be shifted to other taxpayers in the first year (FY 2008).

SB 5256. Property tax exemptions are decided based on an owner's annual disposable income. This bill is intended to lessen the property tax burden on veterans by excluding veteran's benefits from the calculation of disposable income. This will ensure that veteran's benefits do not exclude otherwise qualified property owners from taking advantage of the exemptions provided for them.

State analysts estimate that $2,000 in state school levy revenues will be shifted from veterans to other taxpayers in fiscal year 2008, rising to $4,500 in 2009. In addition, local revenue losses are estimated to be $1,100 in 2008 with shifts to other taxpayers estimated to be $131,400.

Bills to enact the provisions of Initiative 747

HB 1155, HB 1170, HB 2117, SB 5001. While I-747 waits for its day in court, both houses of the Washington state legislature have introduced legislation this session to enact the provisions of I-747. HB 2117 has the largest number of sponsors and so may have the longest legs.

Discussion

With the exception of the bills that would enact the provisions of Initiative 747, all of the relief measures discussed above would reduce the tax burden for some households by shifting taxes onto other households and on to businesses. As we have noted repeatedly in the past, business bears a higher share of the tax burden in Washington than in most other states. These high taxes present a major competitiveness challenge. Measures that would shift a greater share of the property tax burden onto business would exacerbate this problem.

References

O'Sullivan, Arthur, Terri A. Sexton, and Steven M. Sheffrin. 1995. *Property Taxes and Tax Revolts*. Cambridge University Press

Washington Research Council (WRC). 2000. *Preserve Property Tax Uniformity to Maintain Washington's Economic Competitiveness*. http://www.researchcouncil.org/publications_container/proptaxuni.pdf

Text of bills and joint resolutions as well as fiscal analyses (fiscal notes) can be found on the web at http://apps.leg.wa.gov/billinfo/