Washington
Research Council

Policy Brief

PB 97:8

October 10, 1997

Referendum 47: Property Tax Relief and Control

Property tax reform topped the legislative agenda in 1997. Since the revaluation increases of the early 1990's, when housing prices soared in several parts of the state, lawmakers have struggled to produce a balanced property tax relief package.

Referendum 47 represents their solution. The elements of the referendum were originally passed by the legislature in early in the 1997 session and vetoed by Gov. Gary Locke.

For the most part Ref. 47 is simple: it makes permanent the current 4.7% reduction in the state property tax levy and it moderately slows the growth of property taxes in the future. The complexity of the measure is almost entirely in the legislature's attempt to moderate the assessment spikes which often occur as a result of assessment cycles and changing market conditions.

Reduction in the State Rate: In 1995 lawmakers passed a one-year 4.7% reduction in the state levy (about $0.17 per $1,000 of assessed valuation), affecting the 1996 levy. Had they not extended the reduction, taxes would have increased in 1997; therefore, lawmakers acted promptly in January to make permanent the "temporary" reduction in the state rate. In vetoing the permanent reduction, the governor asked the legislature to again pass a one-year extension. They did, he signed. To make the reduction permanent voters would have to pass Ref. 47. If they do not, lawmakers and taxpayers again face the prospect of the tax increase resulting from the expiration of the one-year relief measure.

Modifying the 106% Limit: The 106% limit governs the total revenue from "regular" property taxes that can be raised by any taxing district. The limit does not apply to "special" levies such as the voter-approved local school taxes. The districts are limited to 106% (that is, a 6% increase) of the highest amount levied in the preceding three years plus the prior year's tax rate applied to new construction and improvements. First applied to local levies by the legislature in 1971, when inflation was running at about 6%, the cap was extended to the state levy in 1979.

Ref. 47 would modify the limit for state and local governments. Increases in state property tax collections would be held to the lesser of 100% plus the inflation rate (currently about 3%, making it a 103% limit) or 106%. For local taxing districts with populations of more than 10,000 a supermajority vote of its legislative authority (e.g. council, commission, or board) would be required to exceed inflation, and then only up to levy up to 106%. Districts with populations of less than 10,000 are unaffected.

Valuation Smoothing (15% Value Limitation): The most complicated feature of the referendum, valuation smoothing, is designed to mitigate the tax shock experienced by taxpayers whose property appreciates dramatically. To accomplish this the legislature created a distinction between the assessed value of property (against which taxes are levied) and the appraised value (the assessor's determination of the property's market value).

Under Ref. 47 the annual rate of growth in each property's assessed value is capped at 15% unless the appraised value exceeds assessed value by more than 60%, in which case the increase in assessed value (i.e. tax value) will be one-quarter of the difference. (Note: 15% is one-quarter of 60%.) Under this provision, spikes in property values are phased in over several years.

Costs and Benefits: The Forecast Council estimates that passage of Referendum 47 will reduce state general fund revenue for the 1997-99 biennium by about $195 million. The most recent state revenue forecast boosted projected general fund income to $19.6 billion, nearly $200 million more than estimated in June. Reserves are expected to exceed $820 million, more than 8% of annual general fund expenditures (or 4.2% of projected biennial spending). General fund spending is limited by Initiative 601 to $19.235 billion, about $150 million more than appropriated by the legislature, leaving some $675 million that cannot be spent. (This all assumes Ref. 47 passes.)

At the local level the impacts are harder to pinpoint. Jurisdictions that have not routinely raised revenues to the 106% limit will be relatively unaffected; others will doubtless face increased taxpayer pressure to hold their increases to inflation. Assuming all local governments stay within the inflation limit the calendar year revenue loss for 1998 would be $31.6 million; total regular property tax imposed by local governments for 1997 amounted to about $1,811 million. This total includes taxing districts with fewer than 10,000 residents; the exact number of such districts and their taxing patterns is not known but presumed to be small.

The nonpartisan Senate Ways and Means Committee (SWM) staff has developed reasonable estimates of the benefits to a hypothetical taxpayer. Acknowledging that benefits will vary, SWM calculates the savings accruing to an owner of property valued at $110,000. Certain assumptions are required: the property will increase in value by 5% annually; local governments will not exceed the inflation limit; and there will be a slight tax shift resulting from the 15% value limitation. Under the referendum the state rate is permanently reduced and state property tax collections cannot exceed the lesser of inflation or 106%.

For this taxpayer the first year (1998) benefit would be $46, climbing to $72 in the second year, and steadily increasing to $328 in 2007. The cumulative ten-year impact totals $1,810.

General Observations: The Washington Research Council has consistently evaluated the state's property tax system as among the nation's best. Critical features include: uniformity; fair market appraisals; and the relatively moderate degree to which governments rely on the tax. The property tax burden here is about at the national average. None of the evidence suggests a need for radical change in our property tax system.

Most of the concern in recent years has resulted from the sharp assessment increases of the early 1990s coupled with a steadily rising tax burden. In addition, state revenue growth has added to pressure to provide across-the-board relief to property owners.

The 15% valuation limit has been the subject of some controversy. Gov. Locke, in his veto of the original legislation, wrote: "I personally favor some mechanism for smoothing large spikes in property valuation. This proposal, however, contains ... fatal flaws." He cited technical objections from some county assessors. A more important objection, said Locke, was his belief that the legislation violated the constitutional requirement for uniformity. By relieving some property owners from taxation on the full market value of their property, the valuation cap also results in a tax shift as other property owners pay higher rates to compensate for the lost tax base.

In his remarks to the Washington Research Council (see box) Sen. Jim West said his analysis suggests that any tax shift will be more than offset by the relief provided by the reduction in the state rate and the control of future increases resulting from the change in the 106% limit.

Uniformity of taxation is an important principle in property taxation. It keeps our system fair and simple. Uniformity was required in the original state constitution in 1889 and remains an important constitutional requirement today. Ref. 47 does not amend the constitution. Proponents believe the valuation cap is consistent with the uniformity principle.

Only the state Supreme Court can render a definitive judgment on the constitutionality of the valuation limit. The legal counsel for the state Senate cites case law in suggesting that the Court "could uphold the methodology as a nondiscriminatory, systematic approach applied consistently to all taxpayers to address legitimate public policy concerns." That is, the approach would not violate uniformity.

The key provisions of Ref. 47 are generally consistent with the principles associated with good property tax systems. The reduction in the state rate is simple, uniform tax relief. The provisions relating to lowering the 106% limit are consistent with the 1970's legislation establishing the limit at approximately the inflation rate.

With regard to uniformity the picture is murkier. While it may be constitutional the value limitation represents a departure from strict uniformity and will result in some tax shifting. Improved assessment practices, however, will moderate the likelihood of significant spikes. It's unlikely that the tax shifts will be large or enduring; the limit does not represent the beginning of a classification system.

Modest solutions are often appropriate for minor problems. Ref. 47 represents that kind of balanced, pragmatic approach.

In late September state Sen. Jim West and former governor Mike Lowry presented their views on the referendum at a small forum provided by the Washington Research Council Board of Trustees.

Sen. West, Senate Ways and Means chair and one of the sponsors of the legislation, reviewed the major benefits of the measure: the reduction in the state property tax levy; the modified 106% limit; and the smoothing mechanism. He said passage of the referendum will ease the property tax pressure that often causes voters to oppose local school levies and is an appropriate vehicle for returning some of the state's current budget surplus to citizens and taxpayers. The most important benefits of Ref. 47 lie in the future, he says, referring to the controls on the growth in taxes and valuation limit.

Former Governor Lowry countered saying that the measure cost too much and provided too little relief for an average homeowner ("only about $4.50 a month for Mary and me"), that it unnecessarily reduced the state's budget reserve, and that it continued a pattern of cutting taxes rather than addressing the "growing disparity between those of us doing well and those of us not doing well." Noting that 58% of the state general fund supported education, and 70% of local government (non-school) spending financed law and justice activities, Lowry suggested property tax reductions would jeopardize important programs.

Visit the Washington Research Council's website at http://www.researchcouncil.org for more on property tax and other issues.