2nd Draft

Taxable Value of Residential Property

The proposed amendment to the Colorado Constitution:

- Increases the taxable portion of residential property from the current level of 7.96 percent to 8 percent beginning with 2005 property taxes; and

- Repeals the process for reducing the rate in the future.

Background

Taxable value of property. Property taxes are paid on a portion of a property's value. For residential property, such as homes, condominiums, apartments, and mobile homes, taxes are currently paid on 7.96 percent of the property's value. This percentage is known as the residential assessment rate. For most other property, such as business and retail property, taxes are paid on 29 percent of the value. A property’s value is multiplied by the assessment rate to determine the taxable value. Property taxes are calculated by multiplying a property's taxable value by a tax rate, called a mill levy.

The state constitution sets the procedure for determining the residential assessment rate. The state legislature must change the residential assessment rate when property is revalued so that the amount of taxable residential property remains at approximately 47 percent of the total and all other taxable property makes up about 53 percent. When the value of all residential property statewide rises compared to the value of all other property, the residential assessment rate decreases. Because this has generally been the case since 1986, the residential assessment rate has fallen from 21 percent that year to 7.96 percent currently. If the trend continues, the rate will continue to decline. On the other hand, if the value of all other property rises faster, the constitutional procedure increases the portion of residential property that is taxed. However, a separate constitutional provision requires voter approval for such an increase. This proposal permanently sets the residential assessment rate at 8 percent. The assessment rates for all other property are not affected by the proposal.

Property taxes. In 2002, Colorado homeowners and businesses paid roughly $4.4 billion in property taxes to local governments, such as counties, cities, school districts, and special districts. Slightly over half of this amount went to schools, while approximately one-quarter went to county governments. The remainder was split among other local governments.

Table 1 illustrates how the different residential assessment rate would impact 2005 property taxes paid on the average Colorado home, currently worth $208,000. Because the residential assessment rate is expected to decline in future years, the difference between taxes paid under current law and under the proposal will grow.

Table 1
2005 Average Property Taxes on a $208,000 Home

	Home Value	Assessment Rate	Taxable Value	Taxes
Current Law	$208,000	7.96%	$16,557	$1,198
Proposal	$208,000	8.00%	$16,640	$1,204
Difference	**$0**	**0.04%**	**$83**	**$6**

Arguments For

1) Current law hampers the state's ability to fund services to all taxpayers, especially in difficult budget times. With each decline in the residential assessment rate, the state pays a larger share of school funding. By permanently setting the residential assessment rate at 8 percent, the proposal provides more property tax revenue for schools. If the increase in the state's share of school funding slows, the state will have more flexibility in funding other services for its citizens.

2) By stabilizing property tax revenues, the proposal may help maintain services that residents receive from local governments. When the tax base of a county, city, fire district, library district, or other special district declines, constitutional limits force down property tax revenue used to fund the services these governments provide. Over half of Colorado's counties, many of them in rural Colorado, will have a lower property tax base this year than last year. The most recent decline in the residential assessment rate will contribute significantly to these lower tax bases.

3) The proposal could encourage companies to move to or expand operations in Colorado. Since the current system was adopted, businesses have gone from paying almost one-and-a-half times what an identically valued home paid in property taxes to over three-and-a-half times as much. Without the proposal, this disparity will increase. New businesses increase the property tax base in the areas in which they locate, which could result in lower taxes for other taxpayers.

Arguments Against

1) This proposal increases property taxes paid by Colorado homeowners and rental property owners. Furthermore, the amount of additional property taxes will likely grow each time property is revalued. The current system has saved homeowners an

estimated $6.8 billion in property taxes since 1987. The proposal is unnecessary because residents of counties, cities, and special districts can decide locally, through elections, to increase taxes to pay for desired services.

2) Without the protection in current law, a larger share of property taxes could be shifted to homeowners in the future. Because their share of property values stays relatively constant, homeowners are protected from property tax increases if business property taxes decline. Business property taxes can decline from downturns in the economy or from changes in the law. Under the proposal, lower business property taxes will increase the share of taxes paid by homeowners.

3) Businesses do not usually make location or expansion decisions solely on the potential tax burden of a given location. In fact, many studies have shown that several other factors, including an educated work force and overall quality of life, are higher priorities when making these decisions. In 1983, when the current system began, the property tax burden for businesses was reduced by taxing apartments as residential property and exempting business inventory and agricultural equipment.

Estimate of Fiscal Impact

School funding. The proposal does not change total funding for public schools. However, the state portion of school funding will decrease. Increasing the taxable value of residential property will increase property taxes for schools. When school property taxes increase, the need for state aid to schools decreases. As a result, this proposal will reduce state spending for public schools by $3.4 million in budget year 2004-05 and $23.4 million in budget year 2005-06. This shift from state to local funding would increase as the gap between the 8 percent rate set by this proposal and current law widens. Table 2 shows the estimated decrease in state spending and the estimated increase in property taxes for schools over the next four years.

Table 2
Impact of Proposal on Revenue Sources for Public Schools

Budget Year	State Expenditures	Local Property Taxes for Schools
2004-05	-$3.4 million	$3.4 million
2005-06	-$23.4 million	$23.4 million
2006-07	-$24.1 million	$24.1 million
2007-08	-$26.7 million	$26.7 million

Local government revenue. The increase in overall taxable values would lead to increased property tax collections for most counties, cities, and special districts that have not reached their spending or property tax revenue limits. For local governments that have already reached their property tax revenue limit, it would increase the proportion of taxes paid by residential property owners, while maintaining the same property tax revenue level for the local government.

Other impacts. There are two other potential state impacts resulting from the change in taxable values. State income tax revenues would be slightly lower in budget year 2004-05, and each year thereafter, as a result of increased itemized deductions claimed by those paying higher property taxes. Also, for years in which the senior citizen homestead exemption is in effect, the state's obligation to reimburse local governments would increase.

Impact on taxpayer. Using the statewide average home value of $208,000 and adding projections for value growth, mill levies, and the residential assessment rate over the next several years, property taxes on the average home would be an additional $6 in 2005, growing to $119 in 2009. Table 3 shows the increase in taxes compared to current law.

Table 3
Additional Property Tax on Average Home Under Proposal

Year	Additional Tax
2005	$6
2006	$58
2007	$58
2008	$119
2009	$119