

Taxable Value of Residential Property

1 **The proposed amendment to the Colorado Constitution:**

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

- 4 ◆ Repeals the process for reducing the percentage in the future.

5 **Background**

6 **Taxable value of property.** Property taxes are paid on a portion of a property's value. For
7 residential property, such as homes, condominiums, apartments, and mobile homes, property taxes paid
8 in 2004 will be based on 7.96 percent of a property's value. This percentage is known as the residential
9 assessment rate. For most other property, such as businesses and vacant land, taxes are paid on 29
10 percent of the value. A property's value is multiplied by the assessment rate to determine the taxable value.
11 Property taxes are calculated by multiplying a property's taxable value by a tax rate, called a mill levy.

$$\text{Taxable Value} = \text{Property Value} \times \text{Assessment Rate}$$

$$\text{Property Taxes} = \text{Taxable Value} \times \text{Tax Rate}$$

12 The state constitution sets the procedure for determining the residential assessment rate. This
13 procedure, known as the Gallagher Amendment, requires that the state legislature change the residential
14 assessment rate when property is revalued. This year, the General Assembly was required to set the rate
15 so that residential property was about 47 percent of the state's total taxable property; all other property
16 makes up 53 percent of the total. These percentages change slightly over time as new homes and
17 businesses are built.

18 Under the Gallagher Amendment, when the value of all residential property statewide rises
19 compared to the value of all other property, the residential assessment rate decreases. Because this has
20 generally been the case since 1986, the residential assessment rate has fallen from 21 percent that year to
21 7.96 percent currently. If the trend continues, the rate will continue to decline. On the other hand, if the
22 value of all other property rises faster, the Gallagher Amendment increases the portion of residential
23 property that is taxed. However, a separate constitutional provision requires voter approval for such an
24 increase. This proposal permanently sets the residential assessment rate at 8 percent. The assessment rates
25 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. Though residential property accounts for 47 percent of all taxable property, the percentage of property taxes actually paid by residential property owners varies slightly because of differences in values and mill levies throughout the state.

Table 1 illustrates how the higher residential assessment rate is expected to increase 2005 property taxes paid on the average Colorado home, currently worth \$208,000. Because the residential assessment rate is expected to decline further in future years, the difference between taxes paid under current law and under the proposal will grow. The rate is expected to decrease to 7.60 percent for taxes paid in 2006 and 2007, and 7.25 percent for taxes paid in 2008 and 2009.

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) The Gallagher Amendment hampers the state's ability to fund services to all taxpayers, especially in difficult budget times. For the 2002-03 school year, state aid accounted for nearly 60 percent of school funding. 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 slows this trend. If the increase in the state's share of school funding is lower, the state will have more flexibility in funding other services for its citizens.

- 2) The proposal may help maintain services that residents receive from local governments. When the property tax base of a county, city, fire district, library district, or other special district declines, constitutional limits force down property tax revenue used to pay for 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) A positive business climate is important to Colorado's economic future. The proposal could help retain existing Colorado businesses and encourage other businesses to move to or expand operations in the state. New businesses increase the property tax base in the areas in which they locate, which could result in lower

1 taxes for other taxpayers. Since the current system was adopted, businesses have
2 gone from paying almost one-and-a-half times what an identically valued home paid
3 in property taxes to over three-and-a-half times as much. Without changes to the
4 current system, this disparity will increase.

5 **Arguments Against**

- 6 1) This proposal increases property taxes paid by Colorado homeowners and rental
7 property owners. Furthermore, the amount of additional property taxes will likely
8 grow each time property is revalued, making housing less affordable for all residents.
9 The current system has saved homeowners an estimated \$6.8 billion in property
10 taxes since 1987. The proposal is unnecessary because residents of counties, cities,
11 and special districts can decide through local elections to increase taxes to pay for
12 desired services.
- 13 2) Without the protection in the Gallagher Amendment, a larger share of property taxes
14 could be shifted to homeowners in the future. Because their share of property values
15 stays relatively constant, homeowners are protected from property tax increases if
16 business property taxes decline. Business property taxes can decline from downturns
17 in the economy or from changes in the law. In 1983, when the current system began,
18 the property tax burden for some businesses was reduced by taxing apartments as
19 residential property and exempting business inventory and agricultural equipment.
20 Under the proposal, lower business property taxes will increase the share of taxes
21 paid by homeowners.
22
- 23 3) Colorado already offers a favorable tax structure for businesses. A recent study of
24 business climates cited Colorado as the 12th best state for small businesses.
25 Businesses looking to relocate consider total business taxes in Colorado compared
26 to those of other states. Furthermore, businesses do not usually make location or
27 expansion decisions solely on potential tax burdens. Many studies have shown that
28 other factors, including an educated work force and overall quality of life, are higher
29 priorities when making these decisions.

30 **Estimate of Fiscal Impact**

31 **School funding.** The proposal does not change total funding for public schools. Schools are
32 funded through a combination of state aid and local property taxes. Increasing the taxable value of
33 residential property, as proposed, will increase property taxes, and thus, local funding for schools. When
34 school property taxes increase, the need for state aid decreases. As a result, this proposal is estimated to
35 reduce state spending for public schools by \$3.4 million in budget year 2004-05 and \$23.4 million in
36 budget year 2005-06. This shift from state to local funding would increase as the gap between the 8

1 percent rate set by this proposal and current law widens. Table 2 shows the estimated decrease in state
2 spending and the estimated increase in property taxes for schools over the next four years.

3 **Table 2**
4 **Impact of Proposal on Revenue Sources for Public Schools**

Budget Year	State Expenditures	Additional 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

5
6
7
8
9
10 **Other local government revenue.** The increase in overall taxable values would lead to increased
11 property tax collections for counties, cities, and special districts that have not reached their property tax
12 revenue limits. For local governments that have already reached their property tax revenue limit, it would
13 increase the proportion of taxes paid by residential property owners, while maintaining the same property
14 tax revenue level for the local government.

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

20 **Impact on taxpayer.** Using the statewide average home value of \$208,000 and adding
21 projections for value growth, mill levies, and the residential assessment rate over the next several years,
22 property taxes on the average home would be an additional \$6 in 2005, growing to \$119 more per year
23 in 2008 and 2009. Table 3 shows the increase in taxes compared to current law.

24 **Table 3**
25 **Additional Property Tax on Average Home Under Proposal**

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

