Taxable Value of Residential Property

The proposed amendment to the Colorado Constitution:

- Increases the taxable portion of a home's value from the current level of 7.96 percent to 8 percent beginning with 2005 property taxes; and

- Repeals the requirement for adjusting the rate in the future.

Background

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.

Property taxes are paid on a portion of a property's market value. For residential property, such as homes, condominiums, apartments, and mobile homes, taxes are paid on 7.96 percent of the property's market 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 market value. Property taxes are calculated by multiplying a property's taxable value by a tax rate, called a mill levy.

Taxable value of property. The state constitution sets the procedure for determining the taxable portion of residential property. The state legislature changes the portion when property is revalued so that the statewide proportion of taxable residential property to all taxable property stays constant. When the market value of all residential property statewide rises compared to the value of all other property, the taxable portion of residential property decreases. 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.

Because residential property values have grown faster than all other property values, the residential assessment rate has dropped from 21 percent in 1983 to its current level of 7.96 percent. The rate would continue to decrease if home values increase at a faster pace than values for all other property. This proposal permanently sets the residential assessment rate at 8 percent. The 29 percent assessment rate for most other property is not affected by the proposal.

Table 1 shows how the taxable value of a house and business is calculated using the market values of two Denver-area properties in 1986 and 2003.

Table 1
Property Value Growth

Year	Residential Property			Nonresidential Property		
	Market Home Value	Percent Taxable	Taxable Home Value	Market Office Value	Percent Taxable	Taxable Office Value
1986	$100,000	21.00%	$21,000	$100,000	29%	$29,000
2003	$272,500	7.96%	$21,690	$221,200	29%	$64,150
% Change	**173%**	**-62%**	**3%**	**121%**	**0%**	**121%**

Arguments For

1) The proposed property tax system could encourage companies to move to or expand operations in Colorado. Since the current system was adopted, businesses have gone from paying roughly 40 percent more in property taxes than an identically valued home to over 250 percent more. Without the proposal, this disparity will continue to grow. New businesses increase the property tax base in the areas in which they locate, which could result in lower taxes for other taxpayers.

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, or special district goes down, constitutional limits force down revenue, which could reduce the services these governments provide. The most recent decline in the residential assessment rate will leave over half of Colorado's counties, many of them in rural Colorado, with a lower property tax base than last year.

3) 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 fixing the taxable portion of residential property, the proposal provides a more stable source of local property tax revenue for schools. If the state's share of school funding does not increase as it has been, the state will have more flexibility in funding other services for its citizens.

Arguments Against

1) This proposal increases property taxes paid by Colorado homeowners. Furthermore, the amount of increase will likely grow each time property is revalued. 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) The current system has saved homeowners an estimated $6.8 billion in property taxes. Because the share of property taxes that homeowners pay is fixed, homeowners are protected in the event that business property taxes decline. Without this protection, a larger share of property taxes could be shifted to homeowners in the future.

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 workforce and overall quality of life, are higher priorities when making these decisions. Also, a recent study placed Colorado as the fourth friendliest tax state for businesses.

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. When 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 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. For those 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 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 income tax 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. Property taxes on the average home would be an additional $6 in 2005. If home values and mill levies stayed constant, the additional taxes would rise to $113 in 2009.