BILL # SCR 1042

TITLE: residential property tax; valuation limitation

SPONSOR: Weiers

STATUS: As Introduced

REQUESTED BY: Senate

PREPARED BY: Hans Olofsson

FISCAL ANALYSIS

Description

Conditional upon voter approval, this bill would freeze the value of primary residences and improvements (Class 3 property) at the tax year (TY) 2000 full cash value. If a residence is sold, the value would be readjusted.

The bill would also limit the annual percentage increase in the value of non-residential real property and improvements to 3% except for most centrally valued property. (Centrally valued property is assessed by the Department of Revenue (DOR) and includes, for example, utilities, mines, and telecommunications companies.)

Based on our conversations with a number of county assessors, we infer that the fiscal impact of this bill would not occur until tax year 2006 (or FY 2007 for state budgetary purposes).

Estimated Impact

The JLBC Staff cannot determine the cost of SCR 1042 with certainty due to critical data limitations. However, with the limited data that was available, we estimated that FY 2007 General Fund costs would be $139 million higher under this proposal than under current law. The accuracy of this estimate is uncertain.

The fiscal impact of this bill may potentially be mitigated by the state's Truth in Taxation (TNT) provisions for K-12 funding (A.R.S. §41-1276). Under TNT, the tax rates used to compute Basic State Aid to schools are potentially adjusted each year to account for the growth in the valuation of existing property. The purpose of such rate adjustments is to prevent tax levies from automatically increasing whenever properties appreciate. By reducing growth in property tax collections, the bill would reduce the future cost of the TNT provisions.

Analysis

Generally, under the Basic State Aid formula, the state share of K-12 funding increases whenever the local property tax base decreases. Therefore, in order to estimate the impact of this bill, we must first determine the amount of net assessed valuation (NAV) that taxing jurisdictions would forego under the valuation limitations of SCR 1042.

Based on limited data from DOR's annual publication, *State and County Abstract of the Assessment Roll*, and the levy limit worksheets provided by all counties in Arizona, we estimate that the total NAV loss in TY 2006 (or FY 2007 from a budgetary perspective) would be $(5.8) billion. Of this amount, $(5.4) billion would be attributable to the Class 3 valuation freeze and $(390) million to the 3% annual growth cap for non-residential real property. However, as noted earlier, our estimates are uncertain due to the limited nature of the information provided.

Class 3 Valuation Freeze
Under current law, we project that Class 3 NAV will grow to $24.8 billion in TY 2006. Using data from several sources, we estimate that the valuation freeze under SCR 1042 could reduce this amount to $19.4 billion, a NAV reduction of $(5.4) billion.

To obtain this estimate, we determined the total value for all Class 3 parcels that existed on the 2000 tax rolls. The value for these properties was then held constant in 2001 and thereafter. For homes entered on the tax rolls for the first time in tax years 2001 to 2005, we used data from the Arizona Real Estate Center to estimate their full cash value. In the year they were added, we used the same data to discount the values of these properties to their TY 2000 level.

For TY 2006, we made further adjustments for homes assumed to be sold on the real estate market. The number of such transactions was based on historical trends. This method resulted in an estimated NAV loss of $(5.4) billion.

As a point of comparison, we used a "back-of-the-envelope" estimate produced by the Maricopa County Assessor's Office. This calculation showed that Maricopa County would lose $(3.4) billion in NAV if SCR 1042 were enacted. This figure is 63% of our estimated NAV impact for the entire state. Since Maricopa County's Class 3 full cash value was 68% of the statewide total in TY 2003, we believe that the two estimates are fairly comparable.

3% Growth Cap

To estimate the impact of the 3% growth cap on non-residential real property, we used the levy limit worksheets from the state's 15 counties. These worksheets can be used to separately calculate the annual growth of existing property and new construction for 3 categories: centrally valued property, locally assessed real property, and locally assessed personal property. The 3% growth cap would essentially only apply to the non-residential portion of locally assessed real property. However, the worksheets do not provide enough detail to allow us to determine whether the growth rate for such property exceeds the cap or not. Based on conversations with the county assessors in Maricopa and Pima, however, we infer that it is not unreasonable to assume that the growth rates for residential and non-residential property are roughly the same.

The statewide rate of appreciation for all locally assessed real property in TY 2004 was 5.2%. In this analysis, we assume that the same growth rate will hold for TY 2006. We further assume that in the absence of a cap, non-residential locally assessed real property will grow by the same percentage. By limiting the growth rate of such property to 3%, we estimate that taxing jurisdictions will incur a total NAV loss $(391) million. This means that the total NAV loss for both the residential valuation freeze and the 3% growth cap on other real property is estimated to be $(5.8) billion.

Under the Basic State Aid formula, any legislation that reduces the local property tax base also increases the state share of total K-12 funding. Based on projected growth rates for assessed valuations in FY 2005 and FY 2006, we estimate that a NAV loss of $(5.8) billion in FY 2007 would translate into a Basic State Aid cost increase of $224 million. However, this cost increase would be offset by an estimated savings of $85 million under the Homeowner's Rebate program due to the Class 3 valuation freeze. Thus, the estimated net impact on the General Fund is $139 million. As noted earlier, however, this estimate is uncertain due to the lack of detailed property information. Furthermore, we were unable to determine the potential cost increase for "1% Cap" school districts and revenue reduction for local property taxes distributed to the state General Fund.

Local Government Impact

This bill would shift the tax burden to property owners not directly affected by valuation limitations under SCR 1042 and/or result in property tax losses for local governments.

3/12/04