STATE OF OREGON

Research Report

LEGISLATIVE REVENUE OFFICE

H-197 State Capitol Building
Salem, Oregon 97310-1347

(503) 986-1266

Research Report # 5-99 **October 1999**

SCHOOL LOCAL PROPERTY TAX OPTION
1999 Legislation

INTRODUCTION

In 1997 Ballot Measure 50 amended the constitution to add a new limit to the local property tax system. The Measure 50 property tax limit is usually stricter than the 1990 Measure 5 limit. The difference is generally referred to as the tax "gap". Measure 50 allows use of this gap with various restrictions. School districts could not use the gap without Legislative approval.

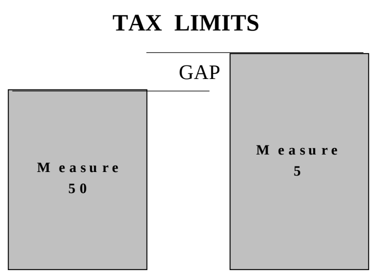
The 1997 Legislature approved use of the gap for a voter approved local property tax option not to exceed $250 per weighted student with a 2003 election sunset. However, the Legislature made implementation conditional on voters not passing a $150 million education lottery bond for facilities, technology and other capital needs. Voters approved the bond so the local option did not take effect.

The 1999 Legislature revisited the issue and passed a local option that is explained in this report. It is somewhat similar to the 1997 version.

The first part of this report describes the various conditions for a local option levy. The second part explains the amount excluded from school formula local revenue. The third part describes the calculation of the maximum local option levy and includes a table with local option and exclusion estimates by school district.

SPECIAL TAX LEVY

A local option tax levy is a special levy subject to many conditions. It is often referred to as a “gap” levy because it can fill the gap between the Measure 50 tax limit and the Measure 5 tax limit. A local option levy is in addition to Measure 50 taxes, but Measure 50 taxes plus any local option taxes cannot exceed the Measure 5 tax limit. A later section provides more information about the gap.



Constitutional Restrictions

Measure 50 includes constitutional restrictions to all property tax levies making use of the gap between Measures 50 and 5 tax limits. The restrictions apply to eligible districts, elections, and length (Article XI Sections (4) and (8)).

- School districts may not impose a local option without legislative approval.
- A majority of voters must approve taxes above the Measure 50 limit.
- A majority of registered voters eligible to vote must vote in any election except a November general election.
- An operating levy cannot exceed 5 years.
- A capital levy cannot exceed the lesser of 10 years or the expected useful life of the capital project.

Statutory Restrictions

ORS 280.040-.145 adds several statutory restrictions to the constitutional restrictions and also incorporates some constitutional restrictions into the statutes.

- Levies for more than a year (serial levies) must be either for
  - a uniform dollar amount each year or
  - the same tax rate each year.
- If a rate serial levy raises more than estimated, the excess revenue is carried over to the next fiscal year.

- Capital projects with life of more than 5 years must be voted on separately from those with a life of less than 5 years.

- Capital projects include buying land or buildings, construction, installation of integral machinery and equipment and furnishings or equipment with a useful life of at least one year.

- Local option taxes may be pledged to repay bonds and voter approval of the local option is approval to issue bonds.

- The election resolution must contain the purpose for the local option, total cost, and number of levy years.

- More than one serial levy can be voted on at the same election, but not more than 4 serial levies may be voted on in a calendar year.

- The ballot must state that approval can increase taxes more than 3 percent and give other information.

Levy Options

The school district can seek approval for either a tax rate or uniform dollar levy local option as mentioned in the first bullet under statutory restrictions. There are several advantages and disadvantages to the rate versus uniform levy based local option.

Levy Base-The local option levy is a fixed dollar amount each year and is converted to a rate by dividing by assessed value.

♦ Advantage: less uncertainty for taxing districts about the amount of taxes that will be collected each year.

♦ Disadvantage: property owners do not know the actual local option tax rate.

♦ Disadvantage: the annual amount can not be increased if the school district has an unexpected increase in costs over the duration of the local option levy.

Rate-Base – The local option tax rate is the same each year and is multiplied by assessed value.

♦ Advantage: property owners know the tax rate and the rate will remain constant over the duration of the local option.

♦ Disadvantage: predicting the total revenue the local option tax rate will generate is difficult. A school district or the local county assessor's office must accurately predict the amount of assessed value the school district will have in the upcoming tax years. The school district will have a shortfall in local option revenues if the actual assessed value falls below the original value estimates and an excess if above the estimate.

EXCLUSION FROM FORMULA LOCAL REVENUE

Local Option Maximum

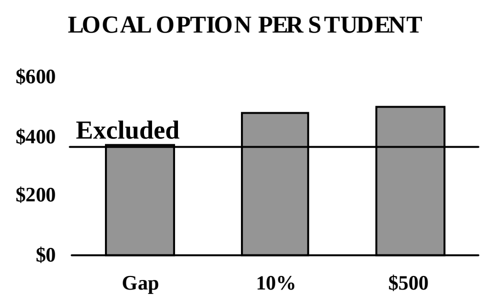
The maximum local option revenue is the amount of the gap. Voters could potentially approve a levy greater than the gap, but it could not be imposed.

Exclusion Limits

The 1999 legislation (HB 2753) excludes local option property taxes from local revenue used in the school distribution formula. The exclusion is the lesser of two limitations:

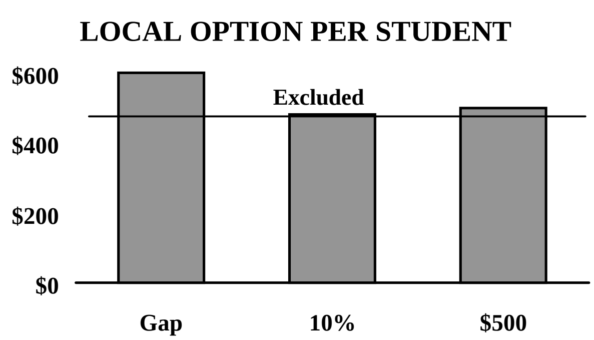
- 10% of school distribution formula revenue (state and local)
- $500 per weighted student (ADMw)

Local option revenue cannot exceed the gap amount so the excluded local revenue is the lesser of the three.



Local Option Exceeds Exclusion Limits

Local option taxes can be more than the exclusion limits. Any revenue above the exclusion does not benefit the school district. If the gap is large enough and voters approve a local option that exceeds the 10% or $500 limits, then the amount above the exclusion limit, if levied, would become part of local revenue utilized by the school formula. The extra district local revenue included would decrease the district's State School Fund dollars. These State School Fund dollars in turn would be allocated to all other school districts if formula revenue statewide is below the legislatively



imposed cap or would not be distributed if above the cap. In effect any local option revenue above the 10% or $500 limits may be shared with all other school districts by how the formula distributes State School Fund dollars.

To help avoid the local option levy exceeding the exclusion limits, a district can levy less than its voter approved local option dollar amount or impose a tax rate lower than the approved rate.

Excludes Tax Received

The local option exclusion from formula local revenue is the amount of taxes actually received by the district, not a tax levy amount. A local option within the gap could potentially be levied higher than the exclusion limit, but tax revenue received be less than the exclusion limit. The discount up to 3% for early payment and delinquencies reduce revenue received. Payments for prior year delinquencies will increase revenue received.

Exclusion Growth

Over time the gap will grow if real market value increases faster than assessed value (see the gap calculation section). As school funding per student increases over time as well, the 10% limit per student will also grow. The average 10% limit estimate is $489 per weighted student in 1999-00. Both the gap and 10% limit will likely grow faster than the percentage increase in number of students. This means that eventually the $500 limit per student is likely to apply in most cases. Legislative changes to the student weighting system or the exclusion limits may alter this expected result.

Multiple Local Options

The revenue excluded from formula local revenue does not have to be from one local option. A district may ask voter approval for multiple local options over several years. These may overlap. A district may seek separate voter approval for different projects. If the gap is the initial constraint, then as the gap grows subsequent local options could be approved within the exclusion limits.

SCHOOL TAX GAP

The tax gap available for school district local options is the difference between the Measure 5 and Measure 50 tax limits. Measure 5 limits the tax for K-12 schools, Educational Service Districts (ESDs) and community colleges to $5 per thousand of real market value. Since Measure 50, each taxing district has a permanent tax rate and some districts have approval for gap bonds.

Both community colleges and K-12 school districts have the option to ask voters for local option levies. With voter approval, local option levies can be imposed in addition to a district's permanent and gap bond taxes, up to the Measure 5 tax limit.

Calculation

The school tax gap amount is calculated on each property according to the following equation.

Tax Gap	=	**Measure 5 Tax Limit** ($5/$1000 times Real Market Value)	-	**Measure 50 Tax Limit** (Sum of permanent and gap bond tax rates times Assessed Value)

The Measure 50 tax is the sum of the permanent and gap bond tax rates for all school districts (K-12, ESDs and community colleges) levying taxes on the property multiplied by its assessed value. If the Measure 5 tax limit is greater than the Measure 50 tax imposed, then a tax gap is available for a local option levy on that property. If the Measure 5 tax limit is less than the Measure 50 tax already imposed, compression (a procedure to proportionately reduce rates to stay within the Measure 5 limit) exists on that property. Then the Measure 50 tax is decreased to the Measure 5 tax and the gap is 0. All individual property gap amounts are summed by code area and then over the school district jurisdiction.

Multiple District Local Options

Community colleges currently have local option authority but ESDs do not. If a community college and school district both have voter approval for local options, the total local option could exceed the gap. In those areas where the community college and school district overlap, rate compression is more likely to occur.

If compression occurs, local option taxes are the first taxes to be reduced. If there is more than one district local option levy, the taxing districts with local option taxes will share any compression losses. The tax gap amount available for a local option is prorated between the two districts using their share of combined local option tax rates.

Implementation

School districts should consult with their local county assessor's office in determining the tax gap available for a local option. A district can use the estimate to assist in answering the following questions: (1) How much to ask for voter approval? (2) Whether the levy should be rate or dollar based? and (3) How to prevent exceeding the exclusion limits?

If the local option tax desired is close to an exclusion limit, a district may want to use an annual levy amount. Revenue collected from this type of levy is more predictable over several years than a rate based local option. Keep in mind that local option revenue above the $500 per student and 10% of formula revenue exclusion constraints does not benefit the district.

Tax Gap Size and Growth

Several factors affect the size of the tax gap and its growth rate.

1. *Real Market and Assessed Values* – If real market value growth is faster than assessed value growth, the tax gap amount increases. Value growth is not evenly distributed around the state and the following factors influence that growth.

    - Strong demand for existing property increases real market value much higher than the 3% a year growth limit for assessed value.
    - High demand for new residential and business construction adds to real market value faster than to assessed value due to most properties' real market value being greater than assessed value.
    - Tax incentive programs (historic, low-income housing, enterprise zones and urban renewal) may increase local investment in certain areas, which leads to higher values.

2. *Community college in district*–A community college district over lapping a school district uses some Measure 50 tax authority that would otherwise increase the gap for a local option.

3. *Level of permanent tax rates* -If the combined K-12 school district, ESD and community college permanent rates are relatively high (above $5), then the gap is smaller compared to an area with lower permanent tax rates and the same values.

4. *Other school taxes allowed* – Some school districts impose gap bonds, which decrease the tax gap amount remaining for a local option levy. If similar other uses for the gap occur in the future, then school local option gaps decline.

5. *Compression* – Addition of a local option rate is more likely to cause tax compression where there was none before and reduce the local option imposed. A small number of code areas with large tax gaps may result in a local option rate that causes compression on properties with only a small tax gap amount when applying the local option tax rate.

6. *Urban* Renewal – See next section.

Urban Renewal (UR) Plans

School districts with urban renewal plans in a portion of their district share their property taxes with urban renewal agencies. School districts, in estimating the amount of local option revenue they will receive, need to make an estimate of their local option taxes allocated to urban renewal agencies. Urban renewal programs affect the tax gap and local options in three distinct ways.

1. Tax Gap increase - An UR agency funds projects that increase real market value and the gap available within the school district.

2. Tax Gap decrease - The taxes imposed by a school district for urban renewal decreases the tax gap. Taxes imposed by school districts for UR agencies are classified as school taxes and subject to the Measure 5 school tax limit. They increase the school district's Measure 50 tax authority used and take a portion of the gap amount available for a local option.

3. Local option decrease – Urban renewal agencies receive a portion of a school local option levy.

Urban renewal's positive effect of increasing real market values in the urban renewal plan area is difficult to quantify. The net effect of the UR program in an area is uncertain.

Table 1 lists all K-12 school districts with urban renewal plans within their district. The total gap estimates include taxes imposed by school districts for urban renewal agencies. This total is then split between the school district and urban renewal agency.

In a large number of cases, the urban renewal plan area does not have a significant amount of tax gap available for a local option tax. The average statewide urban renewal portion is 4.4% of the gap with a high of 23%. The urban renewal portion of the total tax gap is usually less than 10%. This result occurs mainly because classifying a portion of urban renewal's division of tax revenue as school taxes causes properties and code areas within the urban renewal plan to be near or already under tax compression. For some school districts, this classification of urban renewal taxes as school taxes significantly lowers the tax gap. In 1999-2000, the Portland 1J School estimate is $7.5 million for urban renewal revenue classified as Measure 5 school taxes. This is quite a bit more than urban renewal's portion of a future local option if Portland 1J School received approval for a $18.6 million local option. Only $559,432 would be distributed to urban renewal.

Local Option and Exclusion Estimates

Table 2 gives 1999-2000 estimates for K-12 school districts' total and per student gap and the tax rate, per $1,000 assessed value, required to levy their entire tax gap as a local option. These estimates are generated at the code level, not on a property by property basis as an actual local option tax would be evaluated by the county assessor's office. The growth rate assumption is 6%

for assessed value and 9% for real market values over 1998-99 property tax data. The gap estimates assume only a K-12 school local option will be levied. A community college local option would reduce these estimates.

The tax gap is compared to the limits for exclusion from formula local revenue. The last column lists the lower of the three as the highest potential local option levy without exceeding the exclusion limits. This is not the quite the same as the amount collectible without exceeding the exclusion limits.

GLOSSARY

Assessed value (AV): The value set on real and personal property as a basis for imposing taxes. It is the lesser of the property's maximum assessed value or real market value.

Code area: A distinct geographic area having a unique group of taxing districts.

Compression: The process of reducing taxes extended on a property so that the total taxes fall within the Measure 5 limits of $5 per $1,000 real market value for school districts and $10 per $1,000 real market value for general government. Compression is performed on a property-by-property basis.

Division of Tax: One method urban renewal agencies use to collect property tax revenues. A portion of the local districts' taxes in an urban renewal plan area is allocated to the UR agency. The UR portion of taxes is based on the ratio of increment value to total assessed value in the urban renewal plan area.

Gap Bond: District debt service obligations paid for with operating revenues rather than with property taxes from a bond levy. Qualified tax obligations include principal and interest on any bond or formal written borrowing of monies issued before December 5, 1996 backed by a pledge to levy property tax revenues if needed. This category of taxes was established in 1997 with Measure 50. Gap bond tax rates will eventually become part of each district's permanent tax rate.

Increment value: Total assessed value of property in an urban renewal plan area in excess of the frozen value when the plan area was established.

Levy-based local Option: Property tax levy for operating purposes beyond the revenues generated by permanent tax rates. Voters decide on a fixed levy amount to be imposed by taxing districts each year for the local option levy.

Maximum Assessed Value: The taxable value limitation placed on real or personal property by the constitution. It can increase a maximum of 3 percent each year. The 3 percent limit may be exceeded if there are qualifying improvements made to the property.

Measure 5: The constitutional tax limitation passed by Oregon voters in November, 1990. This measure limits the total amount of property taxes allowed on each individual property owner. Schools could impose a tax up to ($5 per $1,000 of real market value of the property) and non-schools could impose a tax of up to ($10 per $1,000 of real market value).

Measure 50: A constitutional property tax rate and assessed value limitation passed by the voters in May, 1997. This measure established a permanent tax rate for each taxing district in the state and for certain districts with voter approval. It established gap bonds, local option and exempt bonds. Assessed values for the 1997-98 tax year were set at 90 percent of the 1995-96 assessed value for each property in the state. Assessed value growth was limited to 3% a year with a few exceptions and can not exceed real market value of the property.

Permanent tax rate: The maximum tax rate a district may use without approval by voters. Districts may use any rate below this maximum. Established in 1997 with Measure 50.

Rate-based local option: Property tax levy for operating purposes beyond the revenues generated by permanent tax rates. Voters decide on a fixed local option tax rate to be applied to their assessed value.

Real market value: The amount in cash that could reasonably be expected by an informed seller from an informed buyer in a transaction between a willing buyer and willing seller as of the assessment date. It is the value used to test the Measure 5 constitutional limits.

Measure 50 tax limit: Amount of property tax each district is allowed to impose on taxpayers as outlined in the constitution or voter approved levies. Under Measure 50, each taxing district has a permanent tax rate authority. Districts could also receive tax authority from gap or exempt bonds or an urban renewal special levy. Some districts also have voter approved local option rate authority. The Measure 50 tax limit is calculated as the sum of all tax rates, subject to Measure 5 limits, multiplied by the assessed value for the district.

Urban renewal agency: The agency responsible for administering urban renewal programs. Cities or counties form urban renewal agencies. They can administer and oversee multiple UR plans and activities within the urban renewal plan area.

Urban renewal plan area: The geographic area in which urban renewal activity takes place. The boundaries of the plan area are established when the plan is formed. This is the area in which the division of tax is calculated to raise revenue for urban renewal agencies.