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F I S C A L   I M P A C T   R E P O R T

SPONSOR Eichenberg **ORIGINAL DATE** 01/21/10 **LAST UPDATED** **HB**

SHORT TITLE Property Tax Limit on Certain Homes **SB** 45

ANALYST Clifford

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY10	FY11	FY12		
	($700.0)		Recurring	General Obligation Bond Capacity

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION

LFC Files

Responses Received From
Taxation and Revenue Department
Department of Finance and Administration

SUMMARY

Synopsis of Bill

Senate Bill 45 would limit the increase in taxable value of residential property for persons 65 years of age or older when they sell a house and purchase another within a 12-month period. Rather than being assessed at its current and correct value – generally the market value – the taxable value would equal the market value of the new house times the ratio of the taxable value of the old house increased by 3 percent divided by the market value of the old house.

FISCAL IMPLICATIONS

Fiscal impacts shown in the table reflect an estimated 0.2% decrease in residential net taxable value and therefore a 0.1% in total net taxable value statewide. State General Obligation Bond Capacity is equal to 1% of statewide net taxable value. The assumptions used in the estimate are outlined below. The estimated G.O. Bond capacity impact shown assumes the proposal would take effect in property tax year 2010. In fact this is unlikely to happen because assessors will already be in the process of finalizing values before the measure takes effect. Thus the estimate is intended only to illustrate the potential magnitude of the capacity impact if the provisions were fully in force. To avoid administrative complexity and the potential for a large number of property value protests, the effective date of the proposal should be clarified and should be for property tax year 2011 at the earliest.

Potential fiscal impacts of the proposal on other property tax beneficiaries are limited because any reduction in taxable value would be offset to a large degree by increases in property tax rates both for operating and debt service levies. Thus, the result would be a shift of tax liabilities from taxpayers 65 years and over to other taxpayers. The total shift appears to be on the order of 0.2% of residential tax liabilities, or about $2 million per year statewide, under the following assumptions: Elderly homeowners represent 13% of all homeowners (U.S. Census Bureau); total residential net taxable value in property tax year 2010 = $31 billion (6% growth from 2009); share of properties transferred each year = 5%; average decrease in taxable value realized = 35%. These figures are likely to be an upper bound on potential fiscal impacts.

DFA reports that some governmental entities have imposed the maximum operating levy authorized by law and their current imposed rate after yield control is also at or near the statutory maximum. These entities would see a decline in their operating revenue if their net taxable value decreases, as could occur under the proposal. Based on the 2009 Certification of Tax Rates, eleven hospitals, two watersheds, DeBaca County, Hidalgo County, City of Vaughn and City of Las Vegas are at the maximum mill rate allowed and remain at or near the same rate after yield control is applied. In addition, eighteen soil and water conservation districts that are not subject to yield control and are imposing the maximum rate allowed by law may see lower operating revenue.

SIGNIFICANT ISSUES

The proposal addresses the "property tax lightning" problem for persons 65 years of age or older. The lightning refers to fact that, whereas property assessments can increase by no more than 3 percent per year while a property is retained by the same owner, assessed value increases to market value when the property is sold. Some commentators have noted that this may deter senior citizens who would otherwise like to "downsize" their homes because their property tax might increase even if the value of the new home is lower. Present law section 7-36-21.3 provides a limitation on property assessments for elderly taxpayers whose income is below specified levels. However, that limit takes effect only after the taxpayer purchases their home. Thus, that section does not protect taxpayers from the tax lightning phenomenon when they buy a house.

PERFORMANCE IMPLICATIONS

By increasing complexity of the property tax valuation system, the proposal may make it harder for assessors to generate accurate property values.

ADMINISTRATIVE IMPLICATIONS

The proposal could introduce significant new administrative burdens for county assessors. If a taxpayer purchases their new house in a different county than the one in which they sell, the assessors of the two counties will have to develop information they can share to effectuate the new formula. Also, all assessors will need to collect information on whether taxpayers are eligible for the new limitation.

TECHNICAL ISSUES

1. The language of the proposal is somewhat inconsistent with the language in present law, and although the language appears to achieve the desired goal, it may create some confusion for property tax administrators. Under present law, taxable value is determined by first determining the assessed value of the house – referred to in statute as the "value of the property for property taxation purposes" -- and then multiplying by a uniform ratio of 1/3 which is required by the constitution. The proposal bypasses the assessed value and calculates taxable value directly from market value. As an alternative, the proposal could multiply the market value of the new house by the ratio of the assessed value to the market value of the old house. The taxable value would then be calculated from the new assessed value in the usual way. The resulting property tax savings would be the same, but the language would be more consistent with current law and practice. The two alternative calculations are illustrated in the following table.

SB 45 as drafted		Present Law	Proposed Law	Difference	
	Old House	New House	New House	Amount	Percent
Market value	$300,000	$200,000	$200,000		
Assessed value	$225,000	$200,000			
Taxable value	$74,250	$66,000	$50,985	-$15,015	-22.8%

Alternative		Present Law	Proposed Law	Difference	
	Old House	New House	New House	Amount	Percent
Market value	$300,000	$200,000	$200,000		
Assessed value	$225,000	$200,000	$154,500		
Taxable value	$74,250	$66,000	$50,985	-$15,015	-22.8%

2. In the proposed ratio of taxable value to market value of the old house, the numerator is increased by 3 percent. This is presumably intended to reflect the increased taxable value of the old house if it had not been sold. The denominator of the formula is the market value of the old house, but it is not clear in which year this market value is to be calculated. For consistency, it would be appropriate to use the market value in the year after the sale. If the market value is used from the year of the sale, then the numerator should not be increased by 3 percent.
3. The proposal does not contain an effective date, which could create confusion for assessors and taxpayers. To allow time for implementation, the provisions could be made applicable to property tax years 2011 and subsequent.
4. The phrase "Except for residential property identified in Section 7-36-21.3 NMSA 1978" is inserted into the beginning of subsection A of section 1 of the bill. This amendment appears to be redundant given the language in present law subsection 7-36-21.2(D).

OTHER SUBSTANTIVE ISSUES

Two judges in the Second District Court have ruled that the present law limitation on assessed value increases in section 7-36-21.2 is unconstitutional because it creates a distinction between taxpayers based on when they purchased their house which is not explicitly authorized in the constitution. The 1998 amendment that created subsection B of Article VIII, Section 1

authorizes the legislature to limit annual increases in property value based on "owner occupancy, age or income." According to TRD, the proposal would also fail to meet the judges' objections because it would still condition property valuation on the date of purchase of a house.

TRD notes that according to the U.S. Census, the proportion of the population age 65 and over varies from a low of 6.9% in McKinley County to a high of 28.3% in Harding County with an average of 12.8% statewide. Thus the effects of the proposal could be expected to vary significantly as well.

ALTERNATIVES

Although the proposal is presumably intended to benefit properties that are the principal residence of the owner, the current language is not limited to owner-occupied residences. Thus, for example, a person 65 years old could sell one rental property and purchase another one and benefit from the provisions.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

Senior citizens, like other house buyers, will continue to face higher taxes than the persons who previously owned the house.

POSSIBLE QUESTIONS

If this proposal is passed, and the rulings of the second district judges are upheld upon appeal, what would be the status of the new provisions?

TC/svb