

FINAL BILL REPORT

HB 2416

C 1 L 07 E1

Synopsis as Enacted

Brief Description: Reinstating the one percent property tax limit factor adopted by the voters under Initiative Measure No. 747.

Sponsors: By Representatives Hurst, Orcutt, Barlow, Roach, Seaquist, Condotta, Kelley, McCune, Goodman, Strow, VanDeWege, Bailey, Wallace, Ahern, Green, Schmick, Lantz, Ross, Springer, Rodne, Morrell, Anderson, Rolfes, Hailey, P. Sullivan, Haler, McCoy, Hankins, Eddy, Priest, Takko, Kristiansen, Blake, Pearson, Ericks, Ericksen, Kessler, DeBolt, Appleton, Skinner, Clibborn, Hinkle, Fromhold, Warnick, O'Brien, Alexander, Campbell, Armstrong, Lovick, Newhouse, Morris, Chandler, B. Sullivan, Schindler, Eickmeyer, Crouse, Jarrett, Dunn, Kretz, Sump, McDonald, Walsh and Linville; by request of Governor Gregoire.

House Committee on Finance

Background:

Property Taxes - Constitutional Limitations. The property tax is the oldest of taxes in Washington and is subject to a number of constitutional and statutory requirements. The state Constitution (Constitution) requires all property taxes to be applied "uniformly;" this has been interpreted to mean that within any given taxing district, the district rate applied to each parcel of taxable property must be the same. The Constitution limits the sum of property tax rates to a maximum of 1 percent of "true and fair" value, or \$10 per \$1,000 of market value. Levies that are subject to the 1 percent rate limitation are known as "regular" levies, and there is no constitutional voting requirement for regular levies. The Constitution does provide a procedure for voter approval for tax rates that exceed the 1 percent limit. These taxes are called "excess" levies. The most common excess levies are maintenance and operation levies for school districts and bond retirement levies. The Constitution provides that excess levies must obtain a 60 percent majority vote plus meet a minimum voter turnout requirement.

Regular Property Taxes - Limit Factor. A district's regular property tax levy is limited by a statutory maximum growth rate in the amount of tax revenue that may be collected annually; this growth rate is known as the limit factor. For districts of 10,000 persons or more, the limit factor is equal to 100 percent plus the rate of inflation, although the governing body of the district (other than the state) may adopt a limit factor of up to 106 percent based on a finding of substantial need. For smaller districts, the limit factor is 106 percent.

Generally, the limit factor requires a reduction of property tax rates as necessary to limit the growth in the total amount of property tax revenue received to the maximum limit factor defined in statute. The limit factor does not apply to new value placed on tax rolls attributable to new construction, to improvements to existing property, to changes in state-assessed valuation, or to construction of certain wind turbines.

While the limit factor constrains regular property tax growth over time, a regular property tax district that chooses to levy an amount that is less than the highest lawful amount allowed under the full limit factor may retain the unused capacity for future use. This is known as "banked capacity." The amount of tax that a district levies in any one year may be more or less than the amount that would otherwise be expected by increasing the previous year's levy by the limit factor. The levy growth depends on whether the district is banking capacity for future use, tapping previously banked capacity, or neither. Many districts have maintained some amount of banked capacity in the past, but since the enactment of Initiative 747 (I-747; see below) the overall amount of banked capacity has diminished.

The limit factor for regular property taxes may be exceeded by voter approval; this process is known as a "lid lift." Lid lifts require approval by a majority of the voters in a taxing district, and allow the district to set its levy in an amount that exceeds the highest lawful amount that could be levied by the district governing body. However, the resulting tax rate must be less than the statutory rate limit.

Constitutional requirements with respect to legislation. The Constitution requires that, regarding legislation, bills contain only one subject, and that subject be contained in the title. The court has interpreted this requirement to mean that there must be rational unity between the subject matter within the measure and that the title adequately reflect the subject matter. The Constitution also requires that current law may not be amended by reference, but rather legislation amending current law must set forth in full the provisions being amended. The primary purpose of this requirement is to inform the public and the Legislature of the nature and effect of proposed changes and to avoid confusion from having disconnected sections scattered throughout the legal code.

History of the Limit Factor and Recent Litigation. The limit factor was formally established in the approval of Referendum 47 (R-47) in 1997. Prior to the passage of R-47, the maximum allowable growth rate for all regular property tax levies had been 106 percent. In approving R-47, state voters restricted taxing districts of 10,000 persons or more to a limit factor of 100 percent plus the rate of inflation, defined to be the change in the implicit price deflator index as determined by the U.S. Department of Commerce. However, districts of 10,000 persons or more other than the state could adopt a limit factor of 106 percent or less with a finding of substantial need by the district's governing body. The limit factor for districts of less than 10,000 persons remained at 106 percent.

In November 2000, state voters approved Initiative 722 (I-722), which among other things changed the maximum limit factor for all taxing districts from 106 percent to 102 percent and eliminated the authority to bank unused taxing capacity. That same month, however, the Thurston County Superior Court enjoined implementation of I-722. In February 2001, the Pierce County Superior Court invalidated the initiative under the title/subject rule. The Washington Supreme Court (Court) affirmed the superior court ruling in September 2001, thus returning law to that approved by the voters under R-47.

In January 2001, I-747 was filed. Under the initiative, the statutory changes under I-722 with respect to the 102 percent limit factor were modified, providing instead a 101 percent limit

factor, unless approved otherwise by a public vote. I-747 also included nonsubstantive language that cross-referenced existing lid lift authority. I-747 did not include modification to the existing authority to bank unused property taxing capacity. In November 2001, two months after the Court invalidated I-722, voters enacted I-747.

In June 2006, the King County Superior Court invalidated I-747, ruling that the initiative violated constitutional requirements concerning amendment by reference. The ruling provided that the persons voting on I-747 were led incorrectly to believe that they were voting to amend the sections of law as amended by I-722 when, in fact, because I-722 had been struck down by the court before voters approved I-747, the voters were voting to amend the sections of law as amended by R-47. In November 2007, the Court affirmed the lower court's ruling, vacating the I-747 changes. Following the ruling, the Department of Revenue issued a memo to county assessors and treasurers providing an interpretation of the ruling. The interpretation provides that the Court's ruling means that regular property taxing districts have additional levying capacity equal to the difference in the hypothetical amount of banked capacity that would have resulted had taxes been levied beginning in 2002 under the limit factor that was established by R-47 and the amount of banked capacity that was accumulated prior to the Court's ruling.

Summary:

Enacting the substantive provisions adopted by the voters under I-747, regular property tax growth levies at the district level are limited to no more than 1 percent growth annually.

The provisions are retroactive to and prospective from taxes levied for collection in 2002. The retroactivity extinguishes the additional levying capacity resulting from the November 2007 Court ruling, but lets stand any banked capacity accumulated prior to the court ruling and the authority to continue to bank future unused capacity.

Votes on Final Passage:

First Special Session

House	86	8
Senate	39	9

Effective: November 29, 2007