Department of Legislative Services

Maryland General Assembly
2010 Session

FISCAL AND POLICY NOTE

House Bill 653 (Delegate Impallaria, *et al.*)
Ways and Means

Taxes - Limitations

This constitutional amendment limits State and local property tax rates on real property to the rates in effect as of November 2, 2010; and limits property tax assessments to the rate of inflation (up to 2%) or deflation beginning with the 2010 full cash value assessment. The amendment also requires the approval from two-thirds of the members elected to each House of the General Assembly in order to pass legislation to increase the rate of an existing tax or impose a tax on an individual or entity not previously subject to the tax.

Fiscal Summary

State Effect: If adopted, potentially significant reduction in general and special fund revenues based on the above provisions. This impact will vary by year, and the result cannot be reliably estimated. State expenditures are not directly affected.

Local Effect: If adopted, potentially significant reduction in local revenues based on the above provisions. This impact will vary by year, and as a result cannot be reliably estimated. Local expenditures are not directly affected. **This bill imposes a mandate on a unit of local government.**

Small Business Effect: Potential meaningful effect on small business property to the extent property tax assessments and tax rates are capped.

Analysis

Bill Summary: The constitutional amendment specifies that the maximum amount of any ad valorem tax imposed on real property by the State, a county, or a municipality may not exceed the rate in effect on November 2, 2010, applied to the full cash value of the real property. Full cash value of real property is defined as the assessor's valuation as shown on the 2010 tax bill; or the appraised value of the property when the property is purchased or newly constructed, or when a change in ownership has occurred, after the 2010 assessment.

However, this limitation does not apply to ad valorem taxes or special assessments to pay the interest on or principal of (1) bonds issued on or before November 2, 2010; (2) bonds for the acquisition or improvement of real property authorized by the General Assembly; or (3) bonds for the construction, reconstruction, rehabilitation, replacement, or capital equipping of school facilities approved by 55% of the voters voting on the proposition.

The amendment specifies that all real property that is not already assessed up to the 2010 full cash value must be reassessed to reflect the 2010 value. The full cash value of property may reflect year to year changes from the base value by the rate of inflation (capped at 2%) or deflation as shown in the Consumer Price Index or comparable data for the area or may be reduced to reflect substantial damage, destruction, or other factors causing a decline in value.

The amendment also requires approval from two-thirds of the members elected to each House of the General Assembly in order to pass legislation to increase the rate of an existing tax or to impose a tax on an individual or entity not previously subject to the tax.

Current Law/Background: The following is a brief discussion of the State's triennial assessment process, the homestead property tax credit program, constant yield tax rate provision, property tax limitation measures, and the Annuity Bond Fund.

Triennial Assessment Process

Under current law, real property is valued and assessed once every three years. This approach, the triennial assessment process, was part of major property tax reform established in 1979. Under this process, assessors from the State Department of Assessments and Taxation (SDAT) physically inspect each property every three years. No adjustments are made in the interim, except in the case of (1) a zoning change; (2) a substantial change in property use; (3) extensive improvements to the property; or (4) a prior erroneous assessment. The assessor determines the current "full market value" of the property and any increase in value is phased in over a three-year period. Any decrease, however, is recognized immediately for assessment purposes.

Because only one-third of the properties in each county is reassessed in a given year, local governments can rely on prior years' growth in the other two-thirds of the base to reduce the full impact of any one-year decline in assessable base. Conversely, when market values are rising, assessed values lag behind the current market, resulting in a slower annual growth in the assessable base than the market may indicate.

Homestead Property Tax Credit Program

The Homestead Property Tax Credit Program provides tax credits against State, county, and municipal real property taxes for owner-occupied residential properties for the amount of real property taxes attributable to annual assessment increases that exceed a specified percentage in any given year. In other words, any increase in taxable assessments each year is limited to a fixed percentage. The cap is set at 10% for State property tax purposes, while local governments have the authority to lower the rate for local property tax purposes. **Exhibit 1** lists the assessment caps for each county. The homestead tax credit program has provided significant local property tax relief in recent years. In fiscal 2010, assessment caps reduced the amount of the county assessable base that is taxable by almost 17%. The corresponding foregone revenue is estimated at $1.4 billion.

Constant Yield Tax Rate

The "constant yield" is a concept that, as property values fluctuate, the tax rate should be adjusted so that the revenue derived from the property tax stays at a constant level from year to year, thus assuring local governments a "constant yield" from its tax source. The constant yield tax rate is the rate that, when applied to the current assessable base, yields the same property tax revenue as in the prior year. Generally, when there is growth in the real property assessable base, the constant yield tax rate is lower than the existing tax rate.

Under the constant yield tax rate law, taxing authorities are required to (1) provide information to the public about the constant yield tax rate and the assessable base and (2) hold public hearings regarding proposals to enact a tax rate that is higher than the constant yield rate. A municipality is exempt from the requirements of the constant yield tax rate law if the difference in revenue generated by the current year's tax rate and the constant yield tax rate is less than $10,000. If a municipality is exempt from the constant yield tax rate law, it is not required to advertise or hold public hearings on the proposed tax rate increase. The municipality may set any tax rate within the limits of its municipal charter. SDAT is required to report to the Attorney General any taxing authority that appears to have violated the requirements of this law. Violating jurisdictions must reduce their property tax rates to the constant yield level and must refund all excessive taxes that have been collected.

Property Tax Limitation Measures

Local property tax limitation measures can affect local property tax rates either by limiting the tax rate a county may impose or by limiting property tax revenue growth. Five counties have provisions in their county charters that limit property tax rates or revenues. Montgomery County limits property tax revenue growth to the increase in the Consumer Price Index (excluding new construction), unless a higher rate of growth is approved by seven of the nine county council members. In Prince George's County, the general property tax rate is capped at $0.96 per $100 of assessed value. Special taxing districts, such as the Maryland-National Capital Park and Planning Commission, are not included under this cap. Anne Arundel County limits property tax revenue growth to 4.5%, or the increase in the Consumer Price Index, whichever is less. In Talbot and Wicomico counties, the total annual increase in property tax revenues is limited to the lesser of 2% or the increase in the Consumer Price Index. Some municipalities also have maximum property tax rates set forth in their charter.

Debt Service and the Annuity Bond Fund

Debt service payments on the State's general obligation bonds are paid from the Annuity Bond Fund. Revenue sources for the fund include State property taxes, premium from bond sales, and repayments from certain State agencies, subdivisions, and private organizations. General funds may be appropriated directly to the Annuity Bond Fund to make up any differences between the debt service payments and funds available from property taxes and other sources. The fiscal 2011 allowance for the Annuity Bond Fund totals $835.2 million.

Background: Proposition 13 (officially titled the People's Initiative to Limit Property Taxation) became an amendment to the California Constitution when it was approved by California voters on June 6, 1978. The U.S. Supreme Court upheld its constitutionality in the case of *Nordlinger v. Hahn, 505 U.S. 1 (1992)*. The most significant portion of the act capped real estate taxes:

> *"Section 1. (a) The maximum amount of any ad valorem tax on real property shall not exceed One percent (1%) of the full cash value of such property. The one percent (1%) tax to be collected by the counties and apportioned according to law to the districts within the counties."*

Passage of Proposition 13 resulted in a cap on property tax rates in the state, reducing them by an average of 57%. In addition to lowering property taxes, Proposition 13 required a two-thirds majority in both houses of the California legislature for future increases in all state tax rates or amounts of revenue collected, including income tax rates. Proposition 13 required a two-thirds majority in local elections for local governments wishing to raise special taxes.

State Fiscal Effect: State property tax revenues may decrease by a significant amount due to the limit on property tax assessments and property tax rates.

The Board of Public Works typically meets in May to set the State property tax rate at an amount to sufficiently meet State debt service requirements. Due to the bill's restrictions, the board may not be able to set a property tax rate sufficient to cover debt service costs. Consequently, the decrease in State property tax revenues will likely require a general fund appropriation to cover debt service on the State's general obligation bonds.

In addition, the requirement that any legislation to increase taxes receive a two-thirds approval in both Houses of the General Assembly could have a significant effect on State general and special fund revenues to the extent necessary revenue measures do not receive the required votes in each House. However, the number of instances when this might occur and the actual effect on State revenues will vary from year to year and cannot be quantified at this time.

Local Fiscal Effect: Restricting the growth in property tax revenues will impact local revenues and will most likely have a negative effect on local government services. The property tax is one of the three major revenue sources for county governments, accounting for 23.8% of total revenues; and the largest revenue source for municipal governments, accounting for 30.5% of total revenues. In fiscal 2010, county governments are projected to collect $6.4 billion in property taxes. The property tax is a relatively stable and predictable revenue source for local governments, and due to the sizeable growth in property assessments in prior years, local property tax collections should remain relatively constant for the near future.

Property assessments in Maryland increased significantly between fiscal 2000 and 2008. The average three-year increase in the full cash value of property undergoing reassessment totaled 5.7% in 2000 and 60.2% in 2006. Properties reassessed for 2007 realized an increase of 56.1% statewide; whereas, reassessments for 2008 realized an increase of 33.2%. However, the continual rapid increase in property assessments halted in 2009, as property valuation declined reflecting the national credit crisis and deteriorating economic conditions. Properties reassessed for 2010 realized a decrease of 16.1%, with only two counties not experiencing a decrease in property reassessments. **Exhibit 2** shows the full cash value increase from January 1999 through January 2010. Property reassessments for 2010 will affect the county's assessable base starting in fiscal 2011.

Exhibit 3 shows the real property assessable base estimate for the tax year beginning July 1, 2010. Assuming county property tax rates remain the same, revenues from the tax on real property are estimated at $6.7 billion in fiscal 2011.

The change is the Consumer Price Index from fiscal 2011 to 2012 is forecast at 2.08%, which exceeds the cap imposed by the bill. Under this scenario, local property tax revenues may not increase by more than 2% from fiscal 2011 to 2012. The bill does provide for certain exceptions to this limitation. However, at this time the effect of any exceptions cannot be reliably estimated, because local property tax rates for fiscal 2011 have yet to be set. It is assumed that local governments will set tax rates to sufficiently meet their respective spending needs.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): State Department of Assessments and Taxation, Property Tax Assessment Appeals Board, Comptroller's Office, Judiciary (Administrative Office of the Courts), Department of Legislative Services

Fiscal Note History: First Reader - February 23, 2010
ncs/hlb

Analysis by: Michael Sanelli

Direct Inquiries to:
(410) 946-5510
(301) 970-5510

Exhibit 1
Homestead Assessment Caps for Maryland Counties

County	FY 2009	FY 2010	FY 2011
Allegany	10%	7%	7%
Anne Arundel	2%	2%	2%
Baltimore City	4%	4%	4%
Baltimore	4%	4%	4%
Calvert	10%	10%	10%
Caroline	5%	5%	5%
Carroll	7%	7%	7%
Cecil	8%	8%	8%
Charles	7%	7%	7%
Dorchester	5%	5%	5%
Frederick	5%	5%	5%
Garrett	5%	5%	5%
Harford	9%	9%	5%
Howard	5%	5%	5%
Kent	5%	5%	5%
Montgomery	10%	10%	10%
Prince George’s	3%	5%	0%
Queen Anne’s	5%	5%	5%
St. Mary’s	5%	5%	5%
Somerset	10%	10%	10%
Talbot	0%	0%	0%
Washington	5%	5%	5%
Wicomico	10%	10%	10%
Worcester	3%	3%	3%

Source: State Department of Assessments and Taxation

Exhibit 2
Triennial Change in Full Cash Value
January 2000 – January 2010

County	2000 Group 3	2001 Group 1	2002 Group 2	2003 Group 3	2004 Group 1	2005 Group 2	2006 Group 3	2007 Group 1	2008 Group 2	2009 Group 3	2010 Group 1
Allegany	4.2%	5.8%	6.2%	9.3%	10.6%	10.6%	21.4%	43.3%	34.5%	16.8%	0.4%
Anne Arundel	8.7%	14.8%	20.4%	37.0%	49.0%	47.6%	65.9%	55.4%	34.9%	-0.3%	-17.9%
Baltimore City	7.3%	10.3%	6.1%	23.0%	18.5%	21.6%	45.6%	58.5%	75.0%	20.9%	-2.6%
Baltimore	4.1%	6.2%	12.1%	11.2%	19.3%	38.1%	53.4%	64.8%	32.6%	13.3%	-13.2%
Calvert	6.0%	8.6%	14.3%	17.6%	29.7%	50.4%	71.7%	69.7%	38.3%	3.1%	-15.1%
Caroline	5.3%	8.5%	12.1%	13.3%	25.0%	38.9%	49.7%	73.6%	40.6%	13.4%	-15.6%
Carroll	6.0%	7.9%	11.7%	15.8%	35.9%	42.2%	54.0%	56.9%	37.4%	5.1%	-19.2%
Cecil	6.7%	9.2%	13.4%	17.4%	20.5%	33.1%	56.7%	54.0%	33.3%	2.5%	-11.0%
Charles	3.7%	6.6%	11.3%	17.9%	27.5%	47.2%	70.2%	62.6%	41.4%	-4.6%	-19.8%
Dorchester	16.8%	8.9%	15.8%	12.3%	19.4%	32.5%	60.8%	58.5%	34.5%	6.8%	-9.9%
Frederick	5.0%	8.8%	13.0%	18.1%	33.5%	56.0%	60.9%	52.2%	27.4%	-4.7%	-22.0%
Garrett	7.6%	8.2%	19.4%	22.2%	11.1%	39.2%	47.6%	38.3%	29.0%	8.5%	0.0%
Harford	4.2%	9.6%	12.8%	14.4%	25.5%	37.6%	48.2%	55.5%	38.6%	9.0%	-14.3%
Howard	6.6%	10.4%	20.1%	29.0%	39.3%	48.5%	58.7%	50.3%	24.2%	-2.3%	-19.8%
Kent	4.0%	17.7%	17.4%	20.7%	30.6%	46.5%	36.8%	65.2%	37.3%	13.5%	-10.3%
Montgomery	6.4%	13.5%	21.8%	36.3%	51.8%	65.0%	63.3%	43.4%	16.2%	-10.6%	-17.0%
Prince George’s	1.9%	4.8%	13.8%	16.4%	32.8%	40.1%	60.6%	79.5%	51.6%	14.6%	-18.4%
Queen Anne’s	8.7%	16.8%	18.3%	38.6%	40.9%	48.3%	58.7%	50.1%	36.8%	7.2%	-12.4%
St. Mary’s	4.3%	6.5%	8.5%	9.7%	19.1%	37.2%	57.2%	84.3%	49.0%	8.2%	-15.5%
Somerset	4.8%	5.8%	6.9%	17.0%	17.1%	49.5%	65.0%	79.6%	45.5%	4.4%	-10.6%
Talbot	11.5%	14.8%	33.6%	34.9%	31.3%	47.9%	53.5%	54.8%	42.7%	13.6%	-9.0%
Washington	6.8%	6.7%	7.1%	11.1%	21.4%	32.4%	58.6%	64.7%	40.2%	3.0%	-18.4%
Wicomico	6.4%	5.2%	6.8%	12.7%	16.9%	21.3%	40.2%	53.2%	40.6%	5.1%	-15.6%
Worcester	6.2%	17.4%	18.0%	70.6%	55.5%	26.7%	78.9%	54.1%	33.3%	-12.7%	-20.0%
Statewide	**5.7%**	**10.1%**	**15.9%**	**26.4%**	**36.0%**	**46.6%**	**60.2%**	**56.1%**	**33.2%**	**0.8%**	**-16.1%**

Source: State Department of Assessments and Taxation

Exhibit 3
County Assessable Base and Estimated Revenues
Fiscal 2011
($ in Thousands)

County	Total County Assessable Base	Net County Assessable Base After Homestead	County Property Tax Rate	Estimated Property Tax Revenue
Allegany	$3,632,987	$3,476,448	$0.9829	$34,170
Anne Arundel	81,356,691	60,285,443	0.8760	528,100
Baltimore City	36,767,495	30,181,504	2.2680	684,517
Baltimore	86,410,221	70,583,002	1.1000	776,413
Calvert	13,344,060	12,640,417	0.8920	112,753
Caroline	3,048,758	2,670,665	0.8700	23,235
Carroll	20,382,147	18,528,234	1.0480	194,176
Cecil	10,726,777	10,232,839	0.9400	96,189
Charles	17,908,318	16,675,284	1.0260	171,088
Dorchester	3,422,933	3,028,538	0.8960	27,136
Frederick	29,572,547	26,570,231	1.0640	282,707
Garrett	4,817,737	4,586,999	0.9900	45,411
Harford	27,660,513	26,210,534	1.0640	278,880
Howard	44,509,507	37,362,990	1.1495	429,488
Kent	3,075,821	2,666,944	0.9720	25,923
Montgomery	175,847,705	170,490,520	0.9160	1,561,693
Prince George’s	96,533,702	74,572,366	1.3190	983,610
Queen Anne’s	8,796,244	7,742,718	0.7700	59,619
St. Mary’s	12,777,368	10,821,540	0.8570	92,741
Somerset	1,714,357	1,641,502	0.9000	14,774
Talbot	10,102,729	7,346,718	0.4320	31,738
Washington	13,552,721	12,380,736	0.9480	117,369
Wicomico	7,115,330	6,857,651	0.7590	52,050
Worcester	17,273,067	16,207,394	0.7000	113,452
Total	**$730,349,735**	**$633,761,217**		**$6,737,229**

Source: State Department of Assessments and Taxation; Department of Legislative Services