South Dakota Legislative Research Council

Issue Memorandum 94-41

INITIATED MEASURE 1:

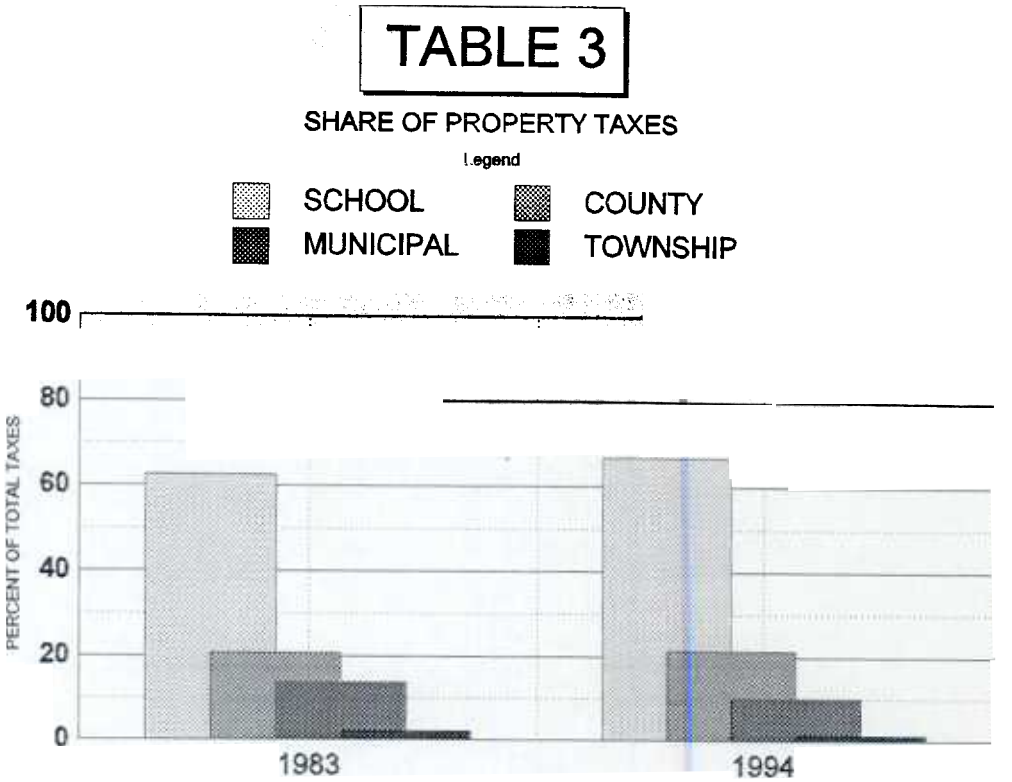
AN INITIATED MEASURE TO REDUCE PROPERTY TAXES

BACKGROUND

Property taxes have long been a target for criticism in this and most other states, and Initiated Measure 1 is not the first attempt to reduce property taxes in South Dakota. In 1935, when the Legislature enacted the sales tax and an income tax, the second section of the bill stated that "This Act shall be known as the 'Property Relief Act', and shall have for its purpose the direct replacement of taxes otherwise to be levied on property." Senate Bill 36, 1935.

Tables 1 and 2 present the yearly increases in total property taxes and the total assessed value from 1983 through 1994. The assessed valuation of the state increased 72% during that period from $12,848,185,265 in 1983 to $22,188,827,811 in 1994. Property taxes increased 93.89% during the same period from $280,918,659 in 1983 to $544,663,818 in 1994. The Consumer Price Index has risen 41.2% from 1983 through 1993. From 1984 through 1993, South Dakota's per capita personal income increased 63.82%, and the total disposable personal income increased 66.4%.

Table 3 presents the four major users of property taxes and the share of property taxes each had in 1983 and 1994. The school and county share of total property taxes increased during that period, and the township and municipal share of the total has decreased.



LEGISLATIVE HISTORY

The 1978 passage of Proposition 13 in California began the latest movement in the United States to limit the growth in taxes and, in particular, taxes on real property. This movement has expressed itself in several ways in South Dakota. In 1980, 1988, and 1990 the people of South Dakota went to the polls to cast their ballots on constitutional amendments to impose limitations on the revenue that could be generated from property taxes. The 1980 and 1988 measures were initiated by the people and the 1990 measure was placed on the ballot by the Legislature. All three measures were defeated.

The 1980 ballot measure (**Dakota Proposition**) would have limited the taxes on real property to one percent of the 1977 full and true valuation. The full and true valuation could experience a yearly inflationary increase of not more than two percent. No additional tax revenue could be raised by the Legislature by changing a tax or creating a new tax unless passed by a two-thirds vote of each house. No new taxes could be imposed on property. Dakota Proposition was defeated with 37.21% voting yes and 62.79% voting no.

The 1988 ballot measure (**Dakota Proposition II**) would have limited taxes on real property to two and one-half percent of the 1984 full and true valuation of each parcel of property except agricultural property, which was limited to one

percent of the 1984 full and true valuation. The full and true valuation could experience a yearly inflationary increase equal to the Consumer Price Index or two percent, whichever was less. Taxes in excess of the limits had to be rolled back over a three-year period. No additional tax revenue could be raised by the Legislature by changing a tax or creating a new tax unless passed by a two-thirds vote of each house. No new taxes could be imposed on property. Dakota Proposition II was defeated with 38.66% voting yes and 61.34% voting no.

The 1990 ballot measure (**Amendment E**) would have limited the annual increase in property taxes. Amendment E was patterned after the property tax freeze the Legislature imposed for the 1990 and 1991 tax years. Amendment E would have, beginning in 1992, limited increases in the revenue that a taxing district could receive from taxes on real property to no more than two percent above the amount received in the preceding year. This two percent limit would have applied only to the real property base that was assessed and taxed in the preceding year. Any improvements or additions to the real property base that were not assessed and taxed in the preceding year would not have been subject to the increase limit. Taxes on any improvements or additions to the real property base that were not assessed and taxed in the preceding year would have been outside the tax limit and would not have been used when calculating the two percent growth limit. Amendment E was defeated with 45.26% voting yes and 54.74% voting no.

There have been many attempts by the Legislature to limit or reduce property taxes, including House Bill 1307 and House Bill 1392 in 1994. Each of these took a different approach to reducing property taxes. House Bill 1307 would have repealed the property tax for education and made change in many other taxes and replaced the revenue with a personal and corporate income tax. House Bill 1392 would have placed on the 1994 general election ballot the question of raising the sales tax and providing a property tax credit with the sales tax revenue. Both bills were defeated.

DISCUSSION

Initiated Measure 1 (**Dakota 1**) affects property taxes in two ways. First, it places a statutory limit on the maximum percentage that property taxes can be of the total value of property. The measure states that "effective January 1, 1995, the tax levy for all agencies cannot exceed 1% of the property's assessed value." Second, the measure limits when, and by how much, property assessments can be changed. The measure states that "real property assessments can only be made when there is a change of ownership, or a new construction completed, and may not be increased by more than 1.25% regardless of the rate of inflation."

The following chart provides the 1993 and 1994 assessed values which are used for calculating the taxes payable in 1994 and 1995, respectively. The chart also provides the total 1994 taxes payable for each county. The 1993 total real property value for taxes payable in 1994 was $21,446,227,225. There are $544,663,818 in property taxes payable in 1994. The 1994 total real property value for taxes payable in 1995 is $22,197,827,811.

This chart also provides the maximum taxes that could have been collected in 1994 and 1995 from a tax of one percent of assessed

reduction in taxes would occur in Fall River County, which would be able to collect in 1995 only 22.65% of the amount collected in 1994. Harding County would have the least reduction in the same comparison; they would be able to collect 69.41% of the amount collected in 1994 in 1995. For the state as a whole, 40.76% of the 1994 taxes could be collected in 1995.

COUNTY	1993 ASSESSED VALUE	1% OF 1993 ASSESSED VALUE	1994 ASSESSED VALUE	1% OF 1994 ASSESSED VALUE	1994 TAXES PAYABLE
AURORA	116,649,837	1,166,498	126,738,418	1,267,384	2,780,020
BEADLE	487,432,208	4,874,322	473,099,069	4,730,991	12,402,813
BENNETT	74,264,491	742,645	75,038,299	750,383	2,283,818
BON HOMME	207,469,982	2,074,700	247,189,885	2,471,899	5,420,441
BROOKINGS	648,917,969	6,489,180	697,006,379	6,970,064	17,147,787
BROWN	1,024,522,612	10,245,226	1,056,531,638	10,565,316	28,345,425
BRULE	185,207,764	1,852,078	206,912,061	2,069,121	4,388,034
BUFFALO	27,022,730	270,227	29,614,941	296,149	629,725
BUTTE	176,632,596	1,766,326	213,283,352	2,132,834	5,555,276
CAMPBELL	98,953,045	989,530	98,425,050	984,251	2,006,564
CHARLES MIX	185,454,146	1,854,541	304,691,611	3,046,916	6,129,187
CLARK	229,605,816	2,296,058	200,233,345	2,002,333	4,636,928
CLAY	341,971,064	3,419,711	341,693,981	3,416,940	8,805,891
CODINGTON	642,462,317	6,424,623	688,551,733	6,885,517	17,135,441
CORSON	102,095,579	1,020,956	100,999,595	1,009,996	2,146,494
CUSTER	168,878,391	1,688,784	170,370,175	1,703,702	5,134,908
DAVISON	369,249,499	3,692,495	360,893,820	3,608,938	11,318,998
DAY	247,736,215	2,477,362	248,935,486	2,489,355	5,546,384
DEUEL	193,633,946	1,936,339	175,703,195	1,757,032	4,549,689
DEWEY	85,884,240	858,842	85,454,657	854,547	1,402,094
DOUGLAS	112,222,277	1,122,223	113,127,018	1,131,270	2,723,668
EDMUNDS	203,903,442	2,039,034	210,064,059	2,100,641	3,469,186
FALL RIVER	123,845,188	1,238,452	130,083,989	1,300,840	5,742,133
FAULK	138,969,933	1,389,699	137,958,420	1,379,584	2,980,136
GRANT	350,980,312	3,509,803	281,985,750	2,819,858	8,328,310
GREGORY	165,221,904	1,652,219	182,533,602	1,825,336	3,949,378
HAAKON	147,712,533	1,477,125	148,285,750	1,482,858	2,438,613
HAMLIN	203,009,797	2,030,098	202,630,553	2,026,306	4,663,021
HAND	196,990,025	1,969,900	222,375,289	2,223,753	4,454,009
HANSON	119,464,814	1,194,648	121,814,297	1,218,143	2,735,660
HARDING	111,617,912	1,116,179	108,048,430	1,080,484	1,556,602

COUNTY	1993 ASSESSED VALUE	1% OF 1993 ASSESSED VALUE	1994 ASSESSED VALUE	1% OF 1994 ASSESSED VALUE	1994 TAXES PAYABLE
HUGHES	419,293,266	4,192,933	465,249,170	4,652,492	12,125,635
HUTCHINSON	291,171,586	2,911,716	310,215,139	3,102,151	7,533,191
HYDE	103,772,391	1,037,724	104,350,001	1,043,500	1,996,765
JACKSON	89,109,786	891,098	104,418,407	1,044,184	1,509,701
JERAULD	84,761,095	847,611	97,634,460	976,345	1,876,091
JONES	88,490,746	884,907	89,177,174	891,772	1,487,073
KINGSBURY	239,555,331	2,395,553	241,683,510	2,416,835	4,859,910
LAKE	343,129,943	3,431,299	347,019,303	3,470,193	8,232,873
LAWRENCE	655,339,845	6,553,398	660,486,656	6,604,867	20,218,244
LINCOLN	581,941,198	5,819,412	636,657,601	6,366,576	13,856,817
LYMAN	224,664,042	2,246,640	219,224,175	2,192,242	3,606,049
MARSHALL	183,339,785	1,833,398	200,823,700	2,008,237	3,836,759
MC COOK	207,590,339	2,075,903	221,355,607	2,213,556	5,334,350
MC PHERSON	161,944,357	1,619,444	143,367,980	1,433,680	3,036,879
MEADE	475,417,845	4,754,178	449,199,764	4,491,998	14,006,723
MELLETTE	53,712,320	537,123	71,957,727	719,577	1,171,427
MINER	131,801,312	1,318,013	131,230,418	1,312,304	3,319,514
MINNEHAHA	3,986,991,590	39,869,916	4,104,012,373	41,040,124	104,584,798
MOODY	296,839,903	2,968,399	299,885,787	2,998,858	6,326,636
PENNINGTON	2,002,612,760	20,026,128	2,103,264,919	21,032,649	62,715,339
PERKINS	172,386,079	1,723,861	171,123,577	1,711,236	4,001,002
POTTER	187,365,954	1,873,660	185,563,266	1,855,633	3,385,480
ROBERTS	271,341,231	2,713,412	269,823,782	2,698,238	6,098,483
SANBORN	109,221,330	1,092,213	106,962,083	1,069,621	2,208,898
SHANNON	13,695,317	136,953	13,874,385	138,744	359,140
SPINK	325,774,642	3,257,746	339,331,059	3,393,311	6,868,358
STANLEY	136,187,801	1,361,878	138,945,810	1,389,458	2,703,617
SULLY	185,785,589	1,857,856	206,978,606	2,069,786	3,299,215
TODD	66,619,343	666,193	69,979,395	699,794	1,150,047
TRIPP	243,601,444	2,436,014	276,209,429	2,762,094	5,794,764
TURNER	340,186,680	3,401,867	342,990,538	3,429,905	7,349,857
UNION	452,573,604	4,525,736	489,466,938	4,894,669	9,938,640
WALWORTH	167,042,231	1,670,422	160,788,292	1,607,883	4,503,980
YANKTON	612,392,991	6,123,930	611,216,284	6,112,163	13,575,681
ZIEBACH	52,590,965	525,910	53,086,649	530,866	985,247
TOTAL	21,446,227,225	214,462,272	22,197,827,811	221,978,278	544,663,818

There has been considerable discussion about the confusing language used in Initiated Measure 1. The measure states that the limitations begin "effective January 1, 1995." Some are confused over which tax year the measure will affect first. The proponents argue that it will first affect taxes payable in 1996. Others argue that since property taxes are due and payable as of the first day of the year, this measure may affect the taxes payable in 1995.

The measure also uses the term "agencies" to describe those governmental units which impose property taxes. That term is not currently used in any way to describe local governments or their relationship with the state. Some argue that since there are no "agencies" which impose property taxes, the measure does not limit any property taxes.

The measure uses the phrase "property's assessed value" without providing a definition of "property." The personal property of centrally assessed companies is taxed in addition to their real property. Since the personal property is "assessed" by the Department of Revenue, the measure would seem to apply to both the personal as well the as real property of centrally assessed companies.

The second part of the measure limits when, and by how much, property assessments can be changed. The measure states that "real property assessments can only be made when there is a change of ownership, or a new construction completed." Currently, real property is assessed each year and adjusted, if necessary, to reflect changes in the market as indicated by an analysis of comparable sales. In addition, changes in value resulting from any improvements made during the year are added. This measure would be a major departure from the process of assessing property that has been in use for many years. Initiated Measure 1 would limit changes to the value or property to only when the ownership changes, or when there is "a new construction." The measure does not define "construction".

In addition to limiting when a change can be made to the tax value of a parcel of property, the measure limits the amount of the increase to no "more than 1.25% regardless of the rate of inflation." This has the potential to result in disparity between taxpayers with similar property. Identical structures will have different tax values and will pay different property taxes based solely on one structure having a change in ownership, although the maximum increase limit of "1.25%" will make the difference small when there is a change in ownership. However, the "1.25%" limit also seems to apply to increases from "new construction." Many additions to structures can exceed 1.25% of value of the original structure. A $25,000 garage added to a $50,000 house after the effective date of the measure would increase the value of the house by $625 ($25,000 * .0125 = $625). The property taxes on the house and garage would be $506.25 ($50,506 * .01 = $506.25). A $50,000 house with a $25,000 garage built before the effective date of the measure would pay $750 in property taxes ($75,000 * .01 = $750). The owner of the second house would pay twenty percent more taxes than the owner of the first house.

An issue that the measure does not address is how to divide the property tax revenue that would remain if it were enacted. Currently, each unit of government has a maximum tax levy that it is permitted to impose. This limit is the guide to how the property taxes collected by the county are to be divided between the taxing units within the county. But, with Initiated Measure 1, there is a maximum limit on the property instead of the unit of government, and there is no direction to the units of government on how they are to share in the one percent maximum limit.

PROS AND CONS

If approved, Initiated Measure 1 will reduce the total property taxes that can be collected. Had it been in effect in 1994, there would have been $330,201,546 less raised from the property tax.

The proponents of Initiated Measure 1 argue that this measure is the only way to force the Legislature to reduce the state's over-reliance on the property tax. They argue that the Legislature will have to reduce the cost of government or replace the property tax with a tax which is more fair. The proponents argue that high property taxes discourage development by making the initial cost too great. They argue that high property taxes make owning a home too expensive for the young and those on fixed incomes.

The opponents argue that this state already has one of lowest overall tax burdens of any state in the nation. They argue that Initiated Measure 1 is simply a way to back into an income tax. They argue that there is no guarantee that the Legislature will be able or willing to replace the lost revenue and that without replacement revenue this measure will have a devastating effect on education by forcing the closure of many schools and the layoffs of many teachers.

CONCLUSION

What is it about the property tax that causes so much discontent? When did the ownership of property stop being an indication of wealth? If property ownership is an indicator of wealth, and for some it clearly is, when was the link between property ownership and ability to pay taxes broken? Since 1935, and especially in the last fourteen years, the people of this state have been trying to change, reduce, or eliminate the property tax. Ever since statehood the property tax has been the primary source of revenue for local governments, and, for many years, it was a major source of revenue for state government.

Initiated Measure 1 is the latest attempt to reduce the property tax. The proponents argue that property taxes are too high, that the property tax is unfairly administered, that it represents too large a proportion of this states tax structure, and that government costs too much money and cutting its source of funding is the only way to make it smaller. The opponents argue that it is dangerous to make such a large reduction in the property tax without also resolving the consequences of the reduction. The opponents argue that the Legislature has been unable to agree on a different tax structure or on how to reduce the growth in government, and there is no guarantee they ever will. The opponents argue that without agreement, education will be devastated.

This issue memorandum was written by Scott C. Peterson, Principal Research Analyst for the Legislative Research Council. It is designed to supply background information on the subject and is not a policy statement made by the Legislative Research Council.