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# How would Measure 7 affect Oregon's tax system?

B.A. Weber and K.M. Seidel

In 1990, Oregon voters passed Measure 5, which fundamentally changed Oregon's tax system. Measure 5 imposes a \$10/\$1000 rate limit on property taxes for nonschool local governments (counties, cities, special districts) and phases in a \$5/\$1000 rate limit on property taxes for schools (school districts and community colleges) by 1995-96 (see figure 1). Measure 5 also requires the state until 1995-96 to replace (from the General Fund) revenue lost to schools because of the rate limit.

This publication explains Measure 7, outlines important features of the current tax system, and discusses how Measure 7 would change Oregon's tax system.

## Measure 7

### What is Measure 7?

Measure 7 is a proposed constitutional amendment that would change the property tax rate limits established by Ballot Measure 5 and require the Legislature to provide relief to residential renters equivalent to the relief given to homeowners in Ballot Measure 5.

The measure was placed on the ballot through the initiative process. If passed, it would take effect in fiscal year (FY) 1994—July 1, 1993 to June 30, 1994.

### What are its major provisions?

There are two:

1. **"Split roll" with new property tax rate limits.** Measure 7 would create a "split roll"—that is, two classes of property for property tax purposes: OOPR (owner-occupied homes; technically, "owner-occupied principal residences") and non-OOPR property (industrial and commercial, residential rental, second homes, agricultural and forest land, and vacant land).

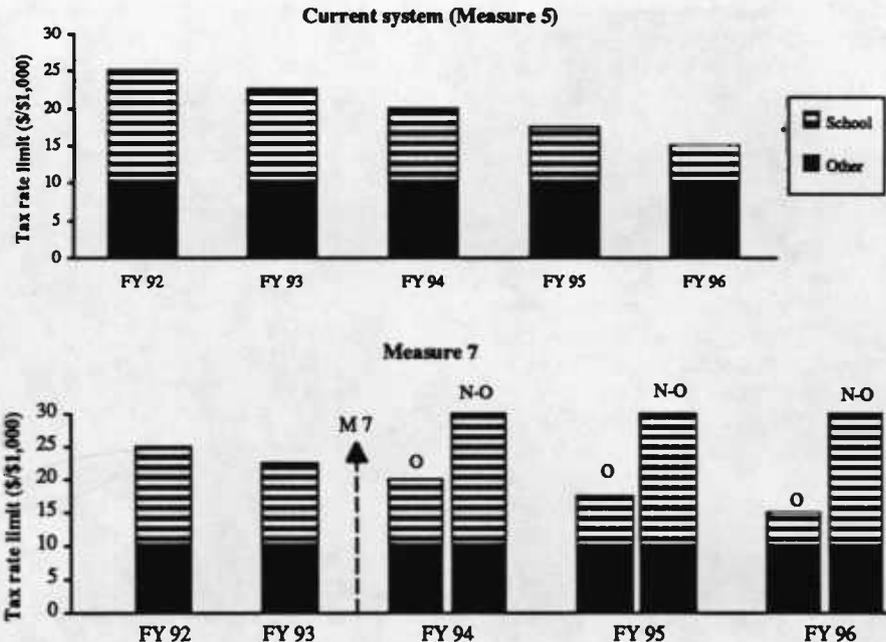


Figure 1.—Property tax rate limits, under the current system (Measure 5) and under Measure 7. O = OOPR; N-O = non-OOPR.

For non-OOPR property, Measure 7 would raise the rate limit for schools to \$20/\$1000 assessed value; it would not change the \$10/\$1000 rate limit for non-schools. (Technically, Measure 7 allows the Legislature to increase the school property tax rate limit on non-OOPR property to \$20/\$1,000, but doesn't require this change in rate limit. Our discussion here assumes that the rate limit is changed.)

For OOPRs, Measure 7 would leave unchanged the rate limits set by Measure 5: \$10/\$1000 assessed value for non-school local governments and a rate limit for schools phasing down to \$5/\$1000 in FY 1996 (see figure 1).

2. **Renter relief.** The measure would also require the Legislature to provide "property tax relief to residential renters

estimated to be equivalent to the relief provided homeowners" under Measure 5. The measure does not specify what "equivalent" relief would be; this would be determined by the Legislature.

Under a reasonable set of assumptions used by the Legislative Revenue Office, equivalent relief would be 5.1% of rent payments in FY 1994, and 9.4% in FY 1996 (when Measure 5 limits have fully phased in for homeowners).

### Do other states have "split rolls"?

About half the states have split property tax rolls. In almost all of these, the different classes of property are

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assessed at different percentages of market value. In these systems, properties of equal market value in different classes pay different property taxes because they are assessed differently, not because they are taxed at different rates.

Another way of implementing a split roll is to apply different tax rates to uniformly assessed property in different classes. Several states have this type of system. Measure 7, which imposes different property tax rate *limits* on different classes of property, is a variant of this type of split roll.

## Property taxes in Oregon's tax system

### *Which governments use the property tax?*

Since 1941, when the State of Oregon ceased levying a state property tax, property taxes have supported only local governments. Revenues from property taxes are the principal source of local general revenue (61% of own-source revenue and 42% of all general revenue in 1990).

Since no local government uses a general sales or income tax as a revenue source, most local jurisdictions depend heavily on the property tax. In FY 1992, the first year in which Measure 5 rate limitations were applied, the total imposed property tax was \$2.5 billion.

Primary and secondary schools received 61.3% of this amount; cities and counties received 15.3 and 11.6%; and the remainder went to special districts (7.3%) and community colleges (4.5%).

### *How has Oregon's property tax burden changed over time?*

The average annual rate of growth of Oregon's property tax levy (net of property tax relief) has been 8.7% since FY 1971. Total personal income has increased by 9.5% per year over the same period. Property taxes have ranged from only 3.3% of personal income in FY 1980 up to 6% in FY 1971.

Since the early 1980s, property taxes have averaged about 5% of personal income. Measure 5 caused the ratio to drop from 5.1% in FY 1991 to 4.9% in FY 1992.

For the past several decades, the direct property tax burden has shifted from business to households. Between FY 1979 and 1992, total property taxes

paid directly by households (after property tax relief and assuming renters pay half the taxes on rental residential property) rose by 95%, in constant dollars.

This happened because of (1) the phasedown and repeal of the major property tax relief programs for homeowners and renters, (2) population growth, and (3) the faster growth of the assessed value of residential property compared with other types of property. During this same period, property taxes paid by Oregon businesses increased by 31%.

In FY 1979, households paid only 40% (after tax relief) of total property taxes. In FY 1992, however, households and businesses each paid about 50% of total property taxes. Between FY 1991 (the last pre-Measure 5 year) and FY 1992, property taxes paid by households rose by 1.6% while business property taxes declined by 8%, in constant dollars.

### *How are property taxes determined in Oregon?*

For any property in Oregon, property taxes are equal to a total property tax rate times the assessed value of the property. The tax rate for a taxing district (city, county, school or special district) is determined each year by dividing the amount of the district's property tax levy (determined in the budgeting process) by the assessed value of all taxable property within the taxing district.

The levy is limited, by a constitutional provision called the "6% limitation," to the "tax base"—that is, a dollar amount that a taxing district can levy each year and that the district can increase by up to 6% a year. Voters can approve levies outside this limit.

Since most property lies within several taxing districts, the tax rates for each district are summed to arrive at a total, or consolidated, tax rate. Measure 5 requires calculation of separate consolidated tax rates for schools and nonschool local governments and places upper limits on these rates as shown in figure 1 (bond levies are exempt from these limits).

If the consolidated rate for either schools or nonschool governments is above Measure 5's rate limit for any property, the tax rate for each district in the category must be reduced so that the consolidated rate is within the rate limit.

This reduces the amount of property taxes imposed by the district.

## Impacts of Measure 7

### *How would Measure 7 affect taxpayers?*

**Homeowners.** Measure 7 would have no direct impact on the amount of property taxes homeowners pay on their homes. This is because Measure 7 doesn't change the phased-in school tax rate limit for owner-occupied homes (OOPRs).

With or without Measure 7, average OOPR property tax rates will decline from \$22.80/\$1000 in FY 1992 to \$13.21/\$1000 in FY 1996.

**Owners of other property.** By raising the school property tax rate limit on non-OOPR property to \$20/\$1000 instead of allowing the Measure 5 phased-in rate limit, Measure 7 would raise an additional \$1.0 billion taxes on these properties during the 1993-95 biennium and \$1.8 billion during the 1995-97 biennium, according to Legislative Revenue Office.

(We're making two critical assumptions: The growth in statewide real market value will be 9% for FY 1993 and 1994, 8% for FY 1995 and 1996, and 7% for FY 1997. The annual statewide growth of school tax levies will be 7%.)

Increases in property taxes for non-OOPR property would be partially offset by declines in income taxes because property taxes are deductible on both corporate and individual income tax returns.

Without Measure 7, average non-OOPR property tax rates will decrease to \$13.21/\$1000.

With Measure 7, average non-OOPR rates would increase from \$22.80/\$1000 in FY 1992 to \$23.05/\$1000 in FY 1996. This would be an increase of \$0.25/\$1000 from current levels. FY 1996 average tax rates on business property would be 74% higher than the tax rates on OOPR.

### *How would Measure 7 affect residential renters?*

The Legislature would be required to establish a program to give renters equivalent tax relief to that received by homeowners under Measure 5.

However, because owners of residential rental property would in most cases be paying somewhat higher property taxes under Measure 7, they

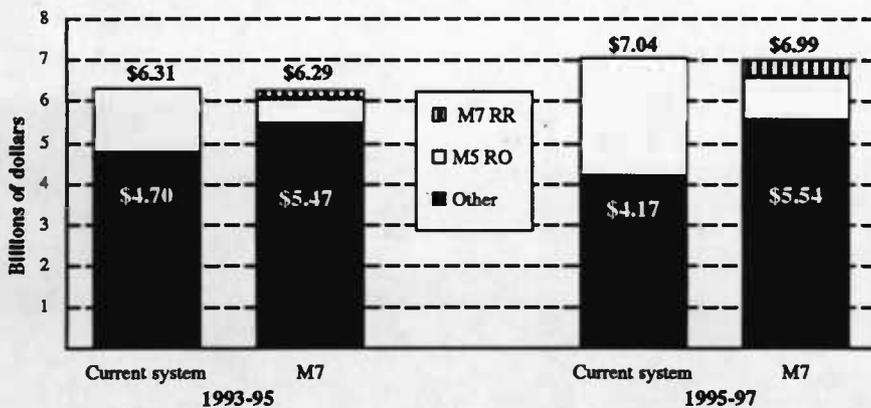


Figure 2.—Impact of Measure 7 on the state General Fund. M7 RR = Renter relief under Measure 7; M5 RO = State's replacement obligation under Measure 5; Other = General Fund not committed to either M7 RR or M5 RO.

might pass on some or all of the increases to renters in the form of higher rents.

#### How would Measure 7 affect state government?

Increased school property tax revenue resulting from Measure 7 would reduce the amount of state payments the General Fund is required to provide to the school system to offset school property tax reductions caused by Measure 5.

The higher property tax collections would reduce the state's replacement obligation on a dollar-for-dollar basis, by \$1,024 million in the 1993-95 biennium and \$1,829 million in 1995-97. However, because property taxes are allowed as a deduction on Federal and state income tax returns, income tax collections by the State of Oregon would decline by about \$28 million in the 1993-95 biennium and \$50 million in 1995-97.

The state would also be required to provide residential renter property tax relief, amounting to an estimated \$235 million in the 1993-95 biennium and \$405 million in 1995-97, according to Legislative Revenue Office estimates.

Measure 7's net impact on the state General Fund would be to reduce the current services budget shortfall, freeing up \$761 million in the 1993-95 biennium for General Fund purposes (see figure 2). This would allow the state to allocate more than it otherwise could to schools under the State School Fund and/or to state services, like corrections, higher education, and human services.

Even though Measure 7 would reduce the state's current service budget shortfall by 60%, the General Fund would still be \$509 million short of being able to fund current services.

During the 1995-97 biennium, Measure 7 would release an additional \$1,374 million for General Fund spending. This would reduce the projected shortfall by 55%.

#### How would Measure 7 affect schools?

Schools would receive more property tax revenue under Measure 7 than under the current system. The current state school aid system would allow for the state to reduce state aid by the amount of school property tax increases. This

would increase the amount the state has available to spend for all General Fund purposes, including schools. It's likely that some of this increase would be allocated to school aid. The result would be an increase in total spending on schools in Oregon.

#### How would Measure 7 affect nonschool local governments?

Measure 7 would change only the school property tax limit established by Measure 5. It would make no change in the limit on nonschool property taxes and related charges (\$10/\$1000 assessed value). Thus, it would have no direct impact on cities, counties, or nonschool special districts.

#### How would Measure 7 affect Oregon's tax ranking?

The two most common ways of ranking states are: taxes per capita (dividing taxes by the state's population) and taxes as a percent of personal income. Oregon is one of only five states without a statewide general sales tax. Because of this, Oregon ranks higher on property taxes than on total state and local taxes.

**Property tax per capita.** In FY 1990, Oregon ranked eighth highest among the 50 states and the District of Columbia. In FY 1996 (when Measure 5 is fully phased in), Oregon will rank 34th if Measure 7 is not passed (assuming other states do not change their tax

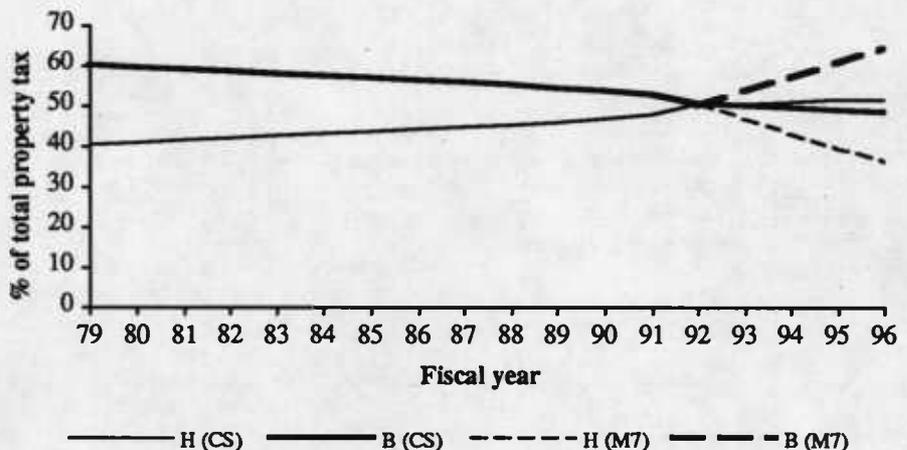


Figure 3.—Household and business shares of property tax (assuming renter households pay half of property tax on rental property and subtracting direct rent relief from household taxes). Source: Legislative Review Office. H(CS) = household share under current system; H(M7) = household share under Measure 7; B(CS) = business share under current system; B(M7) = business share under Measure 7.

systems). With Measure 7's passage, Oregon would rank 18th.

**Property tax revenue as a percent of total personal income.** Oregon ranked 6th in the nation in FY 1990. If Measure 7 is not passed, Oregon will rank 33rd in FY 1996. With Measure 7, it would rank 15th.

**Total state and local taxes per capita.** Oregon's total in FY 1990 was \$1934, 4% below the national average of \$2017. Oregon ranked 20th on this measure in FY 1990. In FY 1996, it would rank 40th if Measure 7 does not pass. With Measure 7, Oregon would rank 31st.

**Total state and local taxes as a percent of personal income.** Oregon ranked 12th in FY 1990. In FY 1996, it would rank 46th if Measure 7 doesn't pass. With Measure 7, it would rank 25th.

#### ***How would Measure 7 affect the fairness of Oregon's tax system?***

"Fairness" is about who pays the taxes. There are two meanings in current usage: (1) fairness among people at different income levels; and (2) fairness between businesses and households.

**1. Income levels.** Many economists consider a tax system to be fair if it is *proportional* (if total taxes as a percent of income are the same for low-income households as for high-income) or *progressive* (if taxes are a lower percent of income for low-income households than for high-income). Oregon's current tax system is roughly proportional.

Measure 7 would provide renter relief, which would tend to make the system more progressive. Whether it would ultimately increase the progressivity of the system would depend on who would bear the burden of the increased business property taxes: consumers (through higher prices), business owners (through lower profits), or employees (through lower wages).

#### **2. Business and household shares.**

Currently, property taxes are split 50-50 between business and households (assuming households pay half of the taxes on rental residential property).

Without Measure 7, there would be a projected 52-48 split between households and businesses by FY 1996.

With Measure 7, in FY 1996, the business sector would pay about 64% of all property taxes and the household sector would pay 36% (after refunds to renters). Figure 3 shows historical and projected trends in the property tax split between households and businesses.

Currently, businesses pay 42% of all state and local taxes. Without Measure 7, businesses would pay 40% of those taxes in FY 1996. With Measure 7, businesses would pay 46% in FY 1996.

#### ***How would Measure 7 affect economic growth?***

There is some disagreement among economists regarding how state and local taxes and services affect state job growth. The net effect of Measure 7 on state job growth depends on which is stronger—the possible *positive* effect of increased state government and school spending or the possible *negative* effect of increased business property taxes.

Evidence from recent studies generally supports two conclusions:

- Taxes have either no significant effect on job growth or a small negative effect.
- Spending on education and infrastructure supported by taxes has a strong positive effect on job growth.

#### ***How would Measure 7 affect local control?***

Measure 7, because it would increase the share of school funding coming from local property taxes relative to state funding, would tend to increase local control of schools.

#### **Summary**

Measure 7 is a proposed constitutional amendment that would:

- Increase the school property tax rate limit on non-OOPR property (property other than owner occupied principal residences) to \$20/\$1000.
- Require the Legislature to provide renter relief equivalent to the property tax relief received by homeowners under Measure 5.
- Reduce the state's Measure 5 obligation to replace school property taxes, thereby allowing more state General Fund resources to be spent on aid to schools and state services.

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