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THE PROPERTY TAX REFORM ACCOUNT

Abstract: This paper provides background information on the Property Tax Reform Account.

Introduction

The Property Tax Reform Account (PTRA) was established by the 1997 Legislature in the Omnibus Tax Act, *1997 Laws of Minnesota*, Chapter 231 for the purpose of building up a source of future funding to continue property tax reform in Minnesota. This paper provides an overview of the PTRA: - estimated funds, permissible fund uses and the Governor's responsibilities under the law. The language of the 1997 law establishing the Property Tax Reform Account (*M.S. 1997 Supplement* 16A.1521) is provided on page 4.

ACCOUNT FUNDING

Based on the Department of Finance's November 1997 revenue forecast, it is estimated that the Property Tax Reform Account will have $872 million on June 30, 1999. The Account's projected funds include:

$46 Million Current Appropriation — The Legislature appropriated $46 million to the PTRA in the 1997 Tax Bill.

$**767 Million Estimated Growth** — The 1997 Legislature earmarked that 60 percent of the November 1997 forecast's positive unrestricted budgetary general fund balance be dedicated to the PTRA. This action translates into $767 million going to PTRA, or 60 percent of the November forecast's unrestricted budgetary general fund balance of $1.279 billion.

$**59 Million Estimated Investment Earnings** — PTRA investment earnings are retained by the account. Current estimates peg the PTRA investment earnings at $59 million, assuming that the entire PTRA account is left unspent through June 30, 1999. Any spending prior to that date will reduce investment earnings.

PERMISSIBLE USES OF ACCOUNT FUNDS

The 1997 law establishing the Property Tax Reform Account provides several options for how account funds may be used to reform the property tax system.

1. Reducing class rates (the percent of market value at which various property types are assessed) to levels now specified as "target" rates in current law:
   a) Commercial/Industrial (market value greater than $150,000) and all Public Utility property from 4% to 3.5%;
   b) Regular market-rate apartments (four or more units and not small city) from 2.9% to 2.5%;
   c) Nonhomestead residential (single units) from 1.9% to 1.25% on first $75,000 and from 2.1% to 1.85% on value over $75,000; or,
   d) further reducing the ratio of the highest class rate to the lowest class rate;
2. Increasing state education aids to reduce property taxes;
3. Increasing the state share of education funding to 70 percent (estimated to be 65.3 percent for FY 1999);
4. Increasing the education homestead credit; or
5. Increasing the property tax refund.

THE GOVERNOR'S RESPONSIBILITIES

The 1997 legislation assigns the Governor with the following responsibilities within the Property Tax Reform Account law:

> *"... the governor shall recommend to the legislature uses of money in the account to compress class rate ratios, while mitigating the shifting of relative property tax burdens from one class to another through the mechanisms listed in clauses (2) through (5).*

Details of the Governor's recommendations to the 1998 Legislature for using funds in the Property Tax Reform Account are not available at this time. On December 2, 1997, the Governor announced that he will pursue a "five-year, $1.7 billion tax cut proposal." The press release accompanying the Governor's announcement indicated that his proposal would include the following property tax elements:

- **#** a "$500 million property tax rebate in 1999."
- **#** a "$748 million in property tax savings through 2003, (including, the compression of the Commercial/Industrial class rate to 3.5 percent)."

Since the Governor's news conference in December, indications are that his preliminary proposals may be extended over a longer implementation time frame or delayed in light of concerns about the effects of Asian economic turmoil on the U.S. and Minnesota economies.

It is expected that the Governor's proposed $500 million property tax rebate in 1999 will be basically the same as the property tax rebate program passed by the 1997 Legislature. A summary of major elements of the 1997 rebate program is given below:

1997 Property tax rebate. Provides a property tax rebate for homeowners and renters equal to 20 percent of property taxes paid in 1997. This rebate is allowed as a refundable income tax credit; it will be claimed on the 1997 income tax return, filed in 1998.

For homeowners, the credit is based on the definition of property taxes that qualify for property tax refund. However, no income restrictions apply and the individual need not own the home on January 2 of the payable year to qualify.

For renters, the credit is 20 percent of rent constituting property taxes, using the property tax refund definition. Under other provisions of the bill, "rent constituting property taxes" is defined as 18 percent of rent paid. Thus, for a renter the rebate equals 3.6 percent of rent paid (20% X 18% = 3.6%). Renters use the certificate of rent paid provided by their landlord to calculate the credit.

The credit for farm homesteads is based on property taxes paid on the house, garage, and 320 acres of farm land. This is the same property tax amount used for determining the property tax refund (circuit breaker).

Individuals who were both renters and homeowners in 1997 can combine the homeowner and rental property taxes in determining the amount of the rebate.

Source: Minnesota House of Representatives Research Department, 1997 Omnibus Tax Law Summary, July 1997.

The Governor's proposed "$748 million in property tax savings through the year 2003," will likely occur largely through the compression of tax rates to the targets currently specified in law (see page 2 for complete listing) and through additional state aid dollars going to support K-12 education. It is expected that the Governor will use an expanded Education Homestead Credit program to partially hold homeowners harmless from the local property tax liability shifts that will occur under his property tax reform proposal. The 1997 Legislature created the Education Homestead Credit program to offset similar shifts that resulted from the property tax reforms enacted in the 1997 session. A summary of major elements of the 1997 Education Homestead Credit program is given below.

1997 Education Homestead Credit. Establishes an education homestead credit program providing each homestead property with a credit equal to 32 percent of the property's general education tax. The credit is limited to $225 per homestead. For agricultural homesteads, the credit applies only to the portion of the tax attributable to the house, garage and surrounding one acre of land. The credit is deducted by the county auditor at the time property tax statements are determined, so that the homeowner is not required to file an application to receive the credit.

Source: Minnesota House of Representatives Research Department, 1997 Omnibus Tax Law Summary, July 1997.

Conclusion

The Legislature will consider the Governor's recommendations and other options for property tax reform and relief with funds from the Property Tax Reform Account in the 1998 session. While current law dedicates the funds in the PTRA may only be spent for property tax reform, proposals to change the law and use PTRA funds for other purposes can be expected. Final decisions on the use of PTRA funds are also likely to be influenced by any changes in the forecast of state general fund revenues and expenditures that is scheduled to be released in February 1998.

The 1997 Property Tax Reform Account Statute

16A.1521 Property tax reform account.

(a) A property tax reform account is established in the general fund.

(b) Amounts in the account are available for and may only be spent to reform the property tax system by:

(1) reducing the class rates to the target rates specified in section 273.13, subdivision 32, or to further reduce the ratio of the highest class rate to lowest class rate;
(2) increasing state education aids to reduce property taxes;
(3) increasing the state share of education funding to 70 percent;
(4) increasing the education homestead credit; or
(5) increasing the property tax refund.

As provided by section 273.13, subdivision 32, the governor shall recommend to the legislature uses of money in the account to compress class rate ratios, while mitigating the shifting of relative property tax burdens from one class to another through the mechanisms listed in clauses (2) through (5).

(c) The balance in the account does not cancel and remains in the account until appropriated for property tax reform. Investment earnings on the account are credited to the account.

HIST: 1997 c 231 art 9 s 2

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