

## How the Class Share System Constrains Policy Options

The class share system was a key component of the 1981 state law (S7000a) that established the city’s current property tax system. In 1989 the method for determining class shares was substantially altered. Starting with each tax class’s share of the overall property tax levy as it stood in 1989, the current version prevents a class’s levy share from increasing by more than a specified percentage, even if the class’s share of market value (i.e. the tax base) is shifting by more than the cap allows.<sup>1</sup> If a tax class’s market value share increases by more than the cap allows in a given year, the excess amount is shifted to the other classes. The resulting shares determine each class’s share of the levy, which is one of the determinants of the tax rate for each class. In the absence of state action, the distributional results from city action to lower the target assessment ratio in Tax Class 1 would be buffered by the workings of the class share system.

The levy class shares—officially known as the Adjusted Base Proportions—are determined through a multistep process that starts with estimates of market values in each class, which is measured by using equalization rates (essentially an average assessment ratio) based on the state’s analysis of valuations on the city’s assessment rolls. The share of total market value for each class is then compared with the prior year’s share. If the increase exceeds the maximum permitted for that year (it is never more than 5 percent) the increase for that class is capped and the excess increase is distributed among the other classes at the City Council’s discretion. The result is a set of revised class percentage change factors. The factors are applied to the prior year’s final class shares to determine the Current Base Proportions, which are updated once the assessment roll for the upcoming year is finalized by the Department of Finance in late May to account for physical changes such as new construction in the upcoming year’s assessment roll to generate Adjusted Base Proportions. These are the class shares that are used to set class levy and tax rates for the upcoming fiscal year.

As part of the budget negotiations between the Mayor’s office and the City Council, the two sides determine whether the city will maintain the overall tax rate of 12.283 percent, the rate since 2009. Assuming this rate is maintained then the size of the total levy is determined by applying the “frozen” overall tax rate to the total amount of billable taxable assessed value on the assessment roll.<sup>2</sup> The size of the levy to be raised from each class is determined by applying the Adjusted Base Proportions to the total levy. Finally, the tax rate for each class is determined by dividing the class’s total levy by the

<b>Lowering Tax Class 1 Target Assessment Ratio While Maintaining Overall Tax Rate Effects Other Tax Classes As Well Due to Class Share System</b>					
<i>Dollars in millions</i>					
<b>Tax Rate</b>	<b>Total</b>	<b>Tax Class 1</b>	<b>Tax Class 2</b>	<b>Tax Class 3</b>	<b>Tax Class 4</b>
Current Policy	12.283%	20.919%	12.612%	12.093%	10.514%
Lower Target to 5 Percent	12.283%	21.427%	12.584%	12.066%	10.490%
Lower Target to 4 Percent	12.283%	23.311%	12.491%	11.977%	10.413%
Lower Target to 3 Percent	12.283%	28.051%	12.316%	11.809%	10.267%
Lower Target to 2 Percent	12.283%	38.797%	12.086%	11.589%	10.076%
Lower Target to 1 Percent	12.283%	72.102%	11.820%	11.334%	9.854%
<b>Tax Levy</b>	<b>Total</b>	<b>Tax Class 1</b>	<b>Tax Class 2</b>	<b>Tax Class 3</b>	<b>Tax Class 4</b>
Current Policy	\$29,446.0	\$4,214.5	\$11,126.3	\$1,841.2	\$12,210.6
Lower Target to 5 Percent	29,383.9	4,208.6	11,101.3	1,837.1	12,183.0
Lower Target to 4 Percent	29,173.2	4,178.8	11,019.4	1,823.5	12,093.1
Lower Target to 3 Percent	28,776.6	4,122.8	10,865.5	1,798.1	11,924.2
Lower Target to 2 Percent	28,253.1	4,048.6	10,662.6	1,764.5	11,701.5
Lower Target to 1 Percent	27,646.6	3,964.1	10,427.8	1,725.6	11,443.9
<b>Change in Tax Levy</b>	<b>Total</b>	<b>Tax Class 1</b>	<b>Tax Class 2</b>	<b>Tax Class 3</b>	<b>Tax Class 4</b>
Current Policy	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Lower Target to 5 Percent	(62.0)	(5.9)	(25.0)	(4.2)	(27.7)
Lower Target to 4 Percent	(272.8)	(35.7)	(106.9)	(17.7)	(117.5)
Lower Target to 3 Percent	(669.4)	(91.7)	(260.8)	(43.2)	(286.4)
Lower Target to 2 Percent	(1,192.9)	(165.9)	(463.7)	(76.8)	(509.1)
Lower Target to 1 Percent	(1,799.3)	(250.4)	(698.5)	(115.6)	(766.8)

SOURCE: IBO analysis of Department of Finance 2019 assessment roll

total billable taxable value in the class.

Because the class shares are determined by the shares of market value rather than shares of assessed value, lowering the assessment ratios in Tax Class 1 would have no immediate effect on the class shares and hence the shares of the levy that each class will bear. (Eventually some or all of the change in tax liability would be reflected in the price of houses and then be captured in the Tax Class 1 aggregate market value and ultimately in the class shares.) In the revenue neutral scenario, the total assessed value in Tax Class 1 changes but not the total market value. Therefore, the calculation of the Tax Class 1 levy would not change. But, with less taxable billable assessed value in Tax Class 1, the tax rate for the class would be higher.

In a scenario where the target assessment is lowered but the resulting change does not have to be revenue neutral there would again be no difference in market values and therefore no difference in the class shares. However, the overall size of the levy would be lower, with the magnitude of the decline depending on the extent of the reduction in the Tax Class 1 target assessment ratio. With a smaller levy, the levy for each class would also be smaller and hence the tax rates would also be slightly lower for Tax Classes 2, 3, and 4. The tax rate in Tax Class 1 would still increase to make up for the assessed value lost to the lower target ratio.

## Endnotes

<sup>1</sup>Beginning with the 1992 assessment roll the maximum annual change in levy shares was set at 5 percent. However, in many years since then the cap has been lowered in order to hold down tax increases for Tax Class 1 and sometimes Tax Class 2 properties. For the 2019 tax year the final tax rates were determined with the cap set at 1.2 percent.

<sup>2</sup>This differs from the process spelled out in the City Charter, which calls for the overall levy to be determined by the amount of money needed to bring the city's budget into balance, once the Mayor has submitted the estimate of other revenues and the City Council has adopted a budget. A frozen rate has been used in most years since 1992. The exceptions were in 2003 and 2004 when the city raised the overall rate by 18.5 percent following the post-9/11 recession and in 2008 and 2009 when the city reduced the overall rate by 7.0 percent but then immediately reversed course in the aftermath of the 2008-2009 recession

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