

## Iowa Property Tax and Local Government Finance Trends

### ISSUE

This **Issue Review** explores the changes in taxable value and average property tax rates from FY 2001 through FY 2014, with breakdowns dividing the changes between urban and rural property and between school district property tax and taxes collected by all other levels of local governments (referred to as nonschool local governments). This **Issue Review** also discusses the changes in revenue received by local governments from local option income and sales taxes over the time period.

### AFFECTED AGENCIES

Local Governments (schools, cities, counties, *etc.*)

The State General Fund through the State School Aid Formula

### PROPERTY TAX BACKGROUND<sup>1</sup>

**Property Classes** – Iowa property is divided into the following property classes:

- Residential
- Agricultural land and buildings
- Commercial
- Industrial
- Railroads
- Gas and electric utilities
- Other utilities

**Agricultural Assessment.** For most types of property, Iowa uses market value as the basis for assessing real property for tax purposes. One exception to market value is the agricultural assessment process. On a county-by-county basis, agricultural property (land and farm buildings) is assessed through a five-year average productivity calculation that uses the landlord's share of revenue from the sale of grain crops from all the agricultural land in the county. Expenses are subtracted from revenue. Net revenue from all agricultural property in the county is divided by the number of agricultural acres and the resulting per acre net earnings value is capitalized at a statutory rate of 7.0%. The result of the calculation is the average assessed value of an acre of farmland in that county. Market value does not play a role in the assessment of agricultural property for tax purposes.

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<sup>1</sup> Resources for detailed explanations of Iowa's property tax system include the [Iowa Department of Revenue](#) and the Legislative Services Agency Legal Services Division publication [Legislative Guide to Local Property Tax](#).

**Rollback.** Iowa property tax law allows for the taxable value of each class of property to increase by no more than 4.0% per year.<sup>2</sup> This limit applies to the revaluation of existing property. To adjust assessed property value to account for this revaluation limit, Iowa has developed a system of assessed value rollbacks. A rollback is the percentage of a property's assessed value that is subject to tax. A rollback of 60.0% means that 60.0% of the assessed value (minus any applicable tax exemptions) of each property within a class is subject to tax that year.

**Ag Tie.** Iowa further limits the growth in taxed value through a statutory tie between agricultural and residential property taxable values. This additional limitation is referred to as the "Ag Tie." The Ag Tie provides that in addition to the 4.0% revaluation limitation, agricultural and residential property are each further limited to no more than the positive growth in taxable value due to revaluation of the other class. Over the years, this additional limit has served to decrease the percentage of residential assessed value that is subject to property tax.

**Tax Rates.** Iowa expresses property tax rates as dollars per thousand dollars of taxed property value. Taxed value equals assessed value, minus any exemptions, times any applicable rollback. A tax rate of \$30.00 means \$30.00 dollars of tax owed per one thousand dollars of taxed value.

**Property Tax Changes (SF 295).** The 2013 General Assembly enacted [SF 295](#) (Property Tax and Income Tax Credit Act). This Act made several changes to the property tax system that has existed since the late 1970s. Major changes include:

- Reduction in the allowed annual statewide revaluation growth rate for residential and agricultural property from the current 4.0% to 3.0%, starting with 2013 assessments (FY 2015).
- Implementation of a special rollback for commercial, industrial, and railroad property equal to 95.0% for FY 2015 and 90.0% for FY 2016 and beyond. Local governments are generally reimbursed for the reduced commercial and industrial taxes that result from the special rollback. The reimbursement is made through a new State General Fund standing appropriation.
- Creation of a new Business Property Tax Credit for properties classified as commercial, industrial, and railroad. The Credit is funded through a State General Fund standing appropriation.
- Creation of a new property class called multiresidential for property that is currently classified as commercial property and is used for human habitation. This new class of property is assigned a declining rollback over several years until it is assigned the same value as the residential rollback in assessment year 2022 (FY 2024).
- Creation of a new property value exemption for telecommunications companies.

**Local Governments.** Iowa allows a number of levels of local governments to tax property. With the exception of a very small amount, State government does not receive any property tax dollars. The levels of local governments include:

- Public school districts (K-12)
- Cities

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<sup>2</sup> The 4.0% limit applies only to the growth due to revaluation of existing property. New construction also adds to taxable value growth and growth due to new construction is not limited. Beginning FY 2015, agricultural and residential revaluation growth will be limited to 3.0% per year. Commercial and industrial property will be assigned a rollback of 95.0% for FY 2015 and 90.0% for FY 2016 and beyond. Note that for utility property the annual revaluation limit is 8.0%.

- Counties
- Community colleges
- Public hospitals
- Agricultural extension
- Assessor offices
- Townships
- Specified special use and special purpose districts

Each level of local government allowed to tax a specific property has its own tax rate. The total of all local tax rates that apply to a single property is referred to as the consolidated tax rate.

### **ECONOMIC CONDITIONS**

Since FY 2001, the State of Iowa and its business owners, farmers, landowners, and homeowners have experienced economic conditions that have significantly impacted both the assessed value of real property and the tax rate at which property is taxed. The most significant changes over that timeframe include:

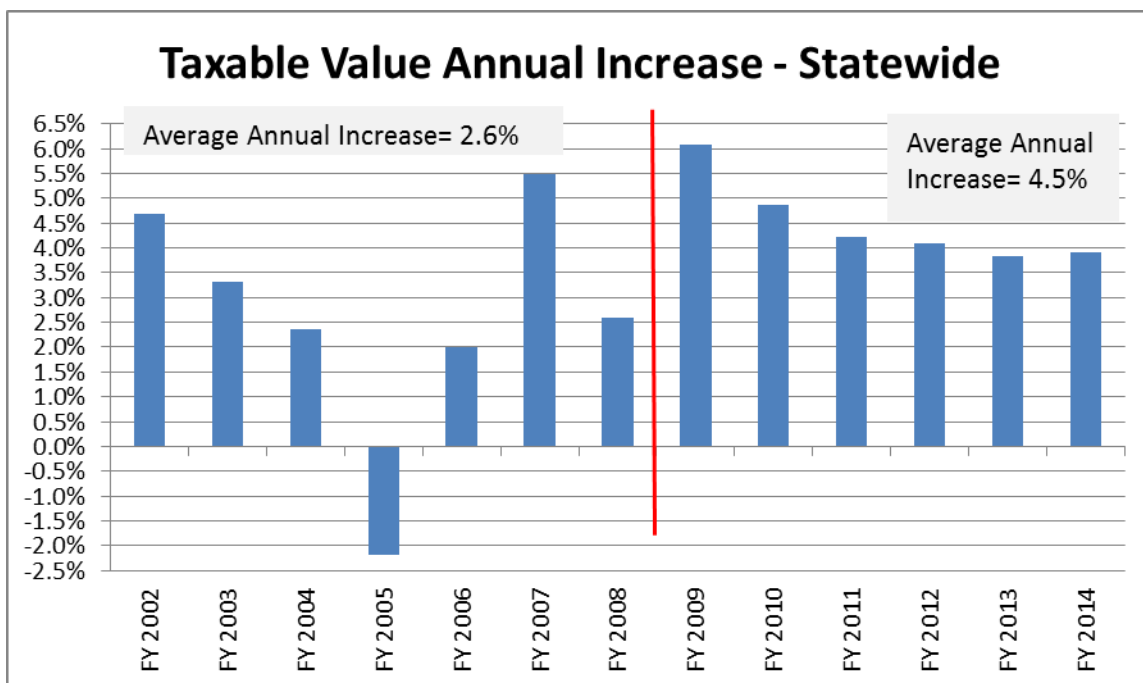
- The creation in the 1990s of local option sales taxes for school districts, cities, and counties to supplement or replace property tax revenue.
- A period of depressed farm commodity prices between crop years 1997 and 2005 resulted in low and negative growth in agricultural land taxable value for fiscal years 2001 through 2008. With very little growth in agricultural taxable value, the Ag Tie kept residential taxable value from increasing during those years, despite the fact that residential property was showing healthy increases in market value at the time.
- As part of the low grain price period, statewide agricultural taxable value declined 18.3% in FY 2005 alone, as two poor crop years (2000 and 2001) replaced two relatively good crop years (1995 and 1996) in the five-year formula used to determine the assessed value of agricultural property.
- A period of significant crop price increases, along with generally improving crop yields from 2007 through 2012, resulted in increased taxable value for agricultural property. These increases allowed the taxable value of residential property to increase as the Ag Tie did not restrict residential revaluation and that class of property was allowed to increase through revaluation by the maximum 4.0% every year.
- A significant period of increasing market value for commercial and residential property starting in the 1990s and lasting through assessment year 2007.
- A major U.S. recession that negatively impacted State General Fund revenue beginning with FY 2009 and resulting in a 10.0% across-the-board appropriation reductions and a major reduction in State General Fund aid to school districts. The reduction took place in FY 2010.
- The U.S. recession also produced stagnant or falling market values for commercial and residential property from assessment year 2008 through 2012. This period also produced significantly less new construction value when compared to earlier years.

### **TAXABLE VALUE**

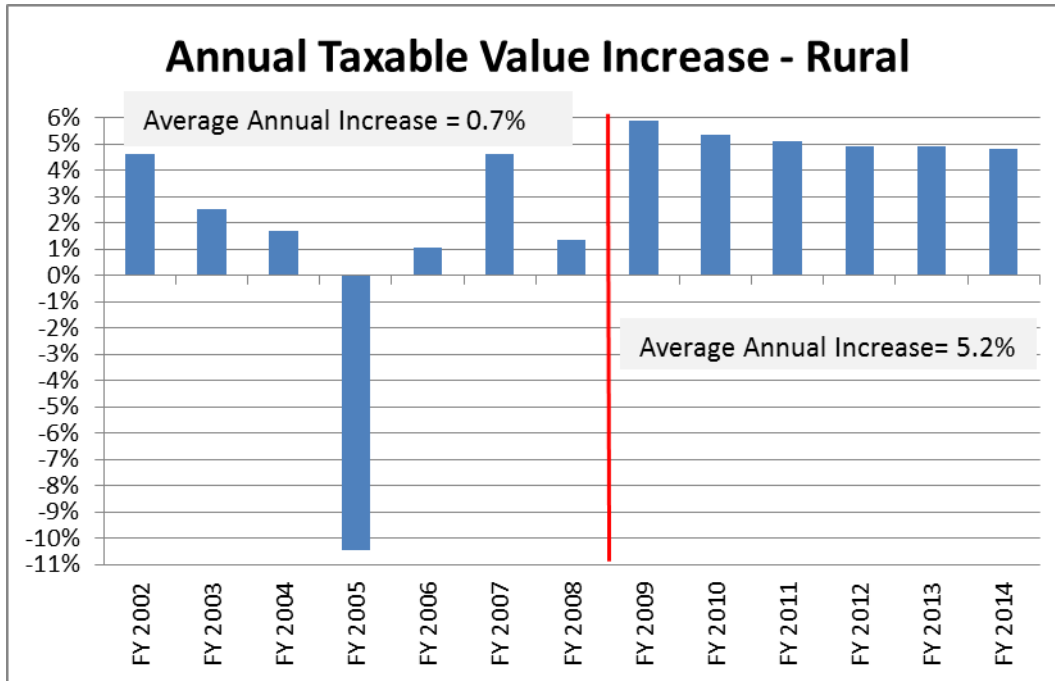
From FY 2001 through FY 2014, taxable statewide property value in Iowa increased at an average annual rate of 3.5%. However, due to the economic issues cited above, the taxable

value growth in the first seven years was quite different from the final six, and taxable value growth in rural areas differed significantly from the growth in urban areas.

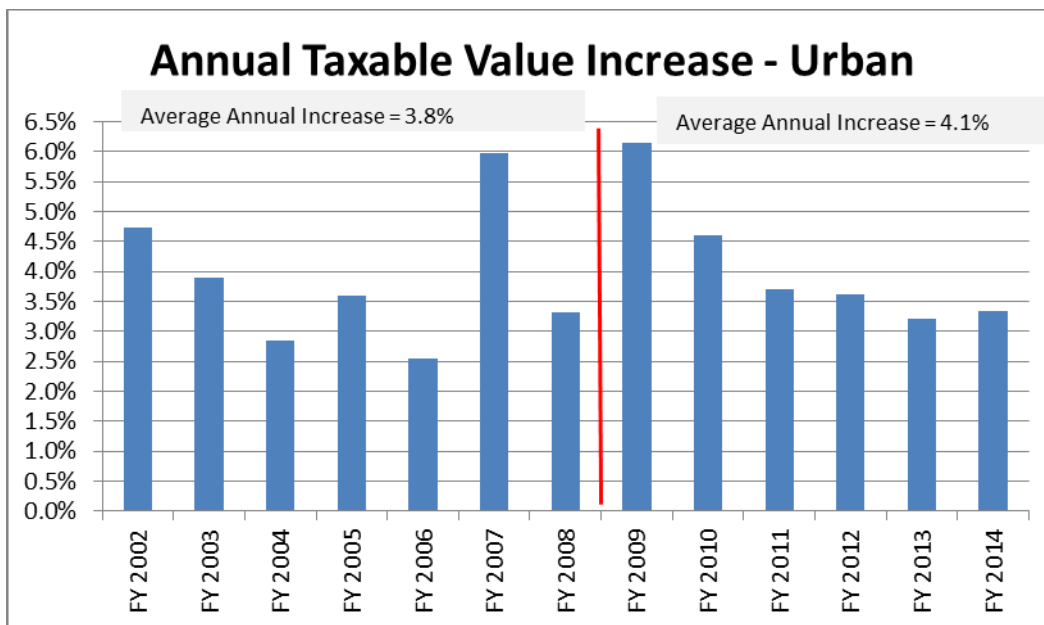
Statewide taxable value growth averaged 2.6% from FY 2001 through FY 2008, and then increased significantly to a 4.5% annual average from FY 2009 through FY 2014. The slow growth of the earlier period came despite the fact that the overall economic conditions of the first period were superior to the conditions of the latter period as the U.S. recession that started in the middle of FY 2008 began to significantly impact the Iowa economy in the first half of FY 2009. In the early period, low grain prices and the Ag Tie held back agricultural and residential taxable value growth, while in the latter period, high grain prices that increased the net income of agriculture allowed agricultural and residential revaluation taxable value gains to overwhelm the negative property value impacts of the recession.



Rural areas are the unincorporated portions of the State, that is, the areas outside of cities. The difference in taxable value growth between the two time periods is even more pronounced when just the rural areas are examined. Taxable value growth in the early period averaged 0.7%, with the period dominated by a 10.5% decrease in FY 2005, brought on by a significant drop in the agricultural productivity calculation that year. In FY 2004, agricultural property represented 56.6% of rural taxable value. The next year, it decreased to 51.6%. Higher grain prices produced higher agricultural productivity values and beginning with FY 2009, agricultural taxable value growth averaged 4.4% or higher each fiscal year. Despite the significant growth in agricultural value in recent years, that class has decreased to 48.6% of all rural taxable value in FY 2014 as the taxable value of residential and industrial property in rural Iowa has grown faster than the taxable value of agricultural property.



There is very little agricultural property in urban areas, so the growth differences between the two periods are much less pronounced. While the Ag Tie did hold down residential taxable value in the early period, positive gains in new construction value kept the taxable value increase relatively high at 3.8%. In the latter period, increases in agricultural productivity kept the Ag Tie from limiting residential taxable value growth at just the time when the recession brought an end to large gains from new construction value.

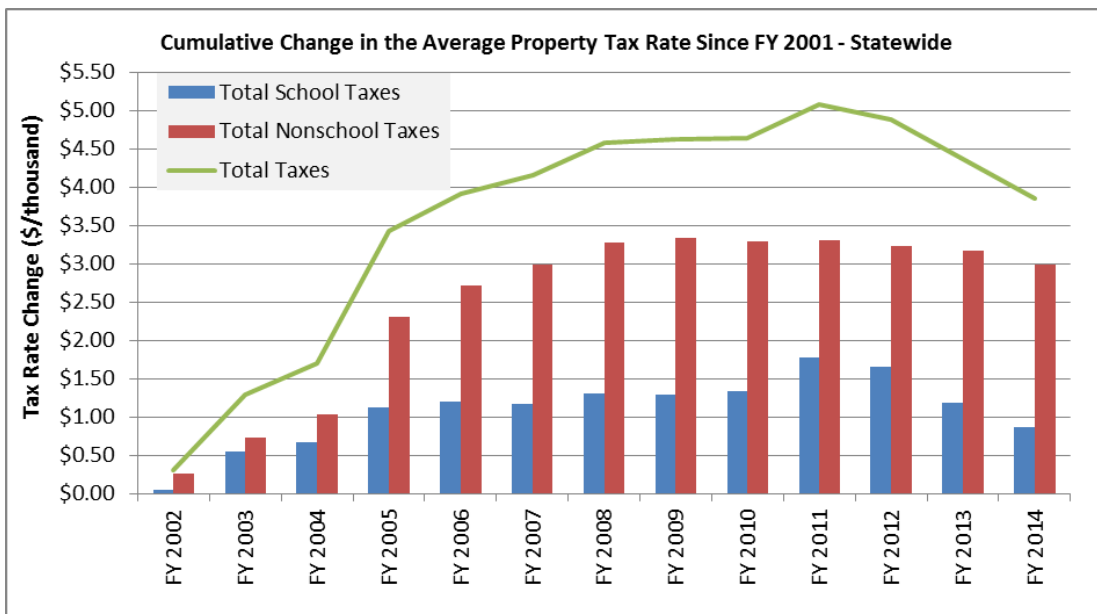


**TAX RATES**

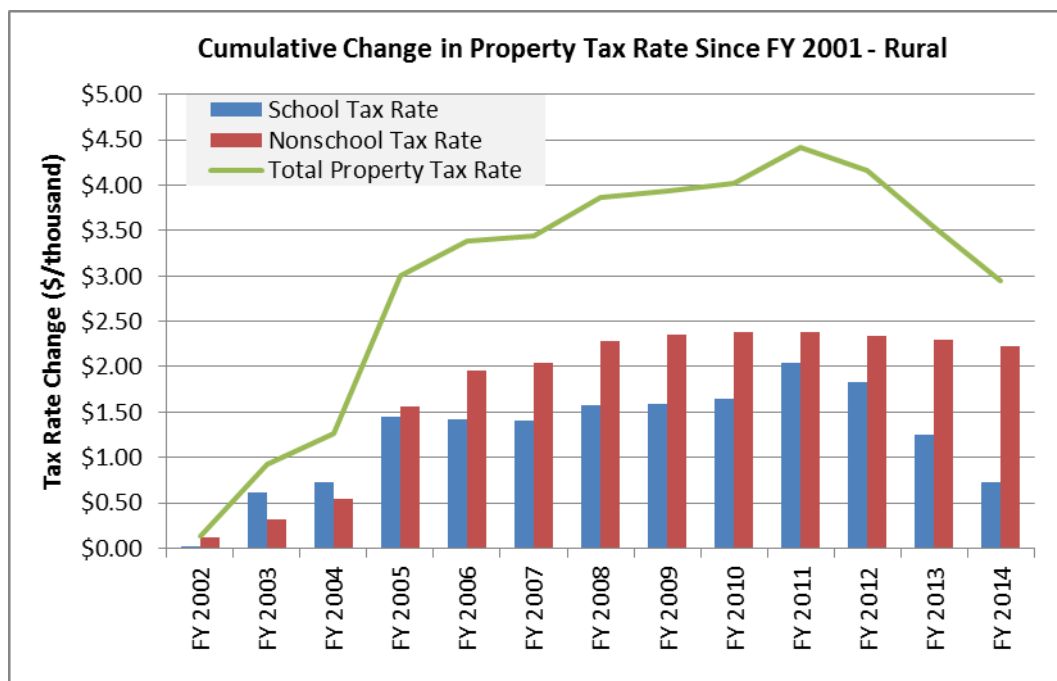
The change in the rate of increase in taxable value appears to have significantly altered the growth in the statewide average property tax rate. The green line on the following chart depicts the growth in the average statewide property tax rate. The line shows that compared to the FY 2001 rate, the average increased \$4.58 in the seven years between FY 2001 and FY 2008. Over the next six fiscal years, when statewide taxable values grew faster, the average property tax rate declined \$0.73.

The bar chart portion of the following chart breaks down the rate increase into a school district portion (blue bars), and all remaining levels of local governments (red bars, labeled "Nonschool"). School districts have a significantly different procedure for taxing property than other types of local governments. The majority of the property tax revenue to be raised in a fiscal year by a school district is set by formula with a significant component of that formula set annually by the General Assembly (allowable growth). Local governments that are not schools do not have budgets established by an outside formula.

The red bars show that as a group, nonschool local governments collectively produced significant rate increases during the low taxable value growth years, and have generally set declining tax rates over the most recent six years when taxable value growth accelerated. For schools, the blue bars show that average rates increased \$1.20 over the first five years. With the exception of FY 2011, average school rates have remained level or declined since FY 2006. The tax rate increase that occurred in FY 2011 was the result of the 10.0% across-the-board appropriation reduction enacted during FY 2010. The State General Fund appropriation to support school district finance was reduced during the fiscal year. In response, schools utilized cash reserves to cover expenditures, and subsequently, they increased cash reserve property tax levies for FY 2011 in order to reestablish cash reserve balances. Since that time, stronger cash reserves, lower allowable growth rates set by the General Assembly, and better taxable value growth have resulted in declining statewide average school tax rates.



Looking at just the rural areas of Iowa shows the impact the FY 2005 drop in agricultural taxable values had on average rural property tax rates. The taxable value decrease caused counties and rural school districts to boost FY 2005 tax rates in order to keep revenue levels from falling significantly. Combined, school and nonschool local governments increased average rural property tax rates \$1.74. Since that time, the average rural school rate has declined back to the FY 2004 level, while the average nonschool rate continued to climb for three more fiscal years before leveling off and then declining slightly. Since peaking in FY 2011, the average rural property tax rate has declined almost \$1.50 and at \$26.07, is now slightly lower than the FY 2005 level.



**Table 1** provides a breakdown of the average school and nonschool property tax rates for urban and rural areas as well as statewide. Rates are presented for FY 2001 (initial year of the data), FY 2008 (the year tax rates peaked), and FY 2014 (final year of the data). The table shows that average property tax rates increased rapidly (\$4.58 statewide) during the years that taxable value grew slowly, and the average rates decreased during the years when taxable value growth accelerated (negative \$0.72 statewide). The overall statewide average property tax rate equaled \$33.41 by FY 2014, \$3.86 (13.1%) higher than the \$29.55 average for FY 2001.

**Table 1****Statewide Average Property Tax Rates - Selected Years**

Rates are in dollars per thousand of taxable value

Rural Areas						
	Average Tax Rate FY 2001	Average Tax Rate FY 2008	Average Tax Rate FY 2014	Rate Change FY 01 to FY 08	Rate Change FY 08 to FY 14	Rate Change FY 01 to FY 14
School	\$ 12.79	\$ 14.37	\$ 13.52	\$ 1.58	\$ -0.85	\$ 0.73
Nonschool	10.33	12.61	12.55	2.28	-0.06	2.22
Total	\$ 23.12	\$ 26.98	\$ 26.07	\$ 3.86	\$ -0.91	\$ 2.95

Urban Areas						
	Average Tax Rate FY 2001	Average Tax Rate FY 2008	Average Tax Rate FY 2014	Rate Change FY 01 to FY 08	Rate Change FY 08 to FY 14	Rate Change FY 01 to FY 14
School	\$ 13.27	\$ 14.37	\$ 14.19	\$ 1.10	\$ -0.18	\$ 0.92
Nonschool	20.89	23.88	23.70	2.99	-0.18	2.81
Total	\$ 34.16	\$ 38.25	\$ 37.89	\$ 4.09	\$ -0.36	\$ 3.73

Statewide - Rural and Urban Areas						
	Average Tax Rate FY 2001	Average Tax Rate FY 2008	Average Tax Rate FY 2014	Rate Change FY 01 to FY 08	Rate Change FY 08 to FY 14	Rate Change FY 01 to FY 14
School	\$ 13.07	\$ 14.37	\$ 13.94	\$ 1.30	\$ -0.43	\$ 0.87
Nonschool	16.48	19.76	19.47	3.28	-0.29	2.99
Total	\$ 29.55	\$ 34.13	\$ 33.41	\$ 4.58	\$ -0.72	\$ 3.86

**TAX REVENUE**

In FY 2001, Iowa local governments collected a total of \$2.856 billion in property tax. In the current fiscal year (FY 2014), they will collect a total of \$5.023 billion. This is an increase of \$2.168 billion (75.9%), and the average annual growth rate is 4.4%. Over the 13 years, school taxes increased at an average annual rate of 4.0%, while nonschool taxes averaged 4.8%.

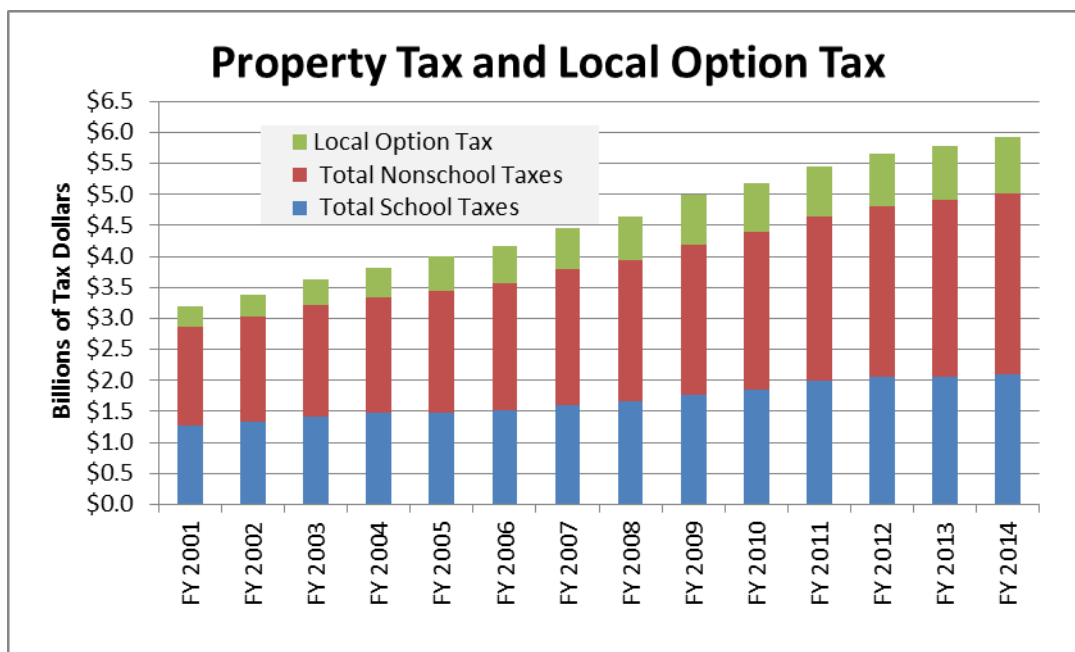
However, this 13-year period witnessed an expansion of local option taxes<sup>3</sup> that provided an additional funding source for the activities of schools, counties, and cities.<sup>4</sup> Combining the two tax revenue streams, Iowa local governments collected a total of \$3.192 billion in property and local option taxes for FY 2001. For FY 2014, they are projected to collect a total of

<sup>3</sup> Local option taxes include the local option income surtax for schools, the hotel/motel tax, the local option sales tax for cities and counties, and the local option sales tax for school infrastructure.

<sup>4</sup> In FY 2001, school districts had the option of imposing a sales tax of up to 1.0% to be used for school infrastructure purposes. By the end of the period, the local option sales tax had become a 1.0% State sales tax, with the revenue from that 1.0% distributed to local school districts. The revenue from this tax is counted in this document as a local option tax for all years.



\$5.919 billion. This is an increase of \$2.727 billion (85.4%), and the average annual growth rate is 4.9%.



The statewide local option tax totals can be converted to property tax equivalent rates by dividing annual local option tax revenue amounts by the statewide taxable value of property for that same year. **Table 2** adds this calculated property tax equivalent number to the statewide tax rate information provided in **Table 1**.

	Average Tax Rate FY 2001	Average Tax Rate FY 2008	Average Tax Rate FY 2014	Rate Change FY 01 to FY 08	Rate Change FY 08 to FY 14	Rate Change FY 01 to FY 14
School	\$ 13.07	\$ 14.37	\$ 13.94	\$ 1.30	\$ -0.43	\$ 0.87
Nonschool	16.48	19.76	19.47	3.28	-0.29	2.99
Local Option	3.48	6.14	5.96	2.66	-0.18	2.48
Total	\$ 33.03	\$ 40.27	\$ 39.37	\$ 7.24	\$ -0.90	\$ 6.34

**Table 2** shows that the local option tax property tax equivalent rate was equal to \$3.48 in FY 2001, and the rate was \$5.96 in FY 2014, an increase of \$2.48. This brings the overall tax rate increase over the 13 years to \$6.34, or 19.2% higher than the FY 2001 tax rate.

**SUMMARY**

Over the past 13 years, changing economic conditions have significantly influenced the pattern of taxable value growth in Iowa. Local governments responded to a low taxable value growth

period by raising tax rates, and responded to the higher taxable value growth period by lowering property tax rates. The impact on tax rate growth from changes in taxable value is more pronounced in the rural areas of the State due to the volatility of agricultural value when compared to other classes of property.

Nonschool local governments raised rates significantly from FY 2001 through FY 2008 in order to maintain revenue growth. For school districts, this process is generally automatic as their demand for property tax dollars is in large part controlled by a State funding formula and annual action of the General Assembly.

Since the 14-year period covered by this *Issue Review* also witnessed an expansion in the use of local option tax revenue to supplement or supplant property tax revenue, a more complete analysis needs to include both local option and property tax revenue sources. Also, over the same time period, the combination of local option tax revenue and property tax revenue produced 4.9% average annual revenue growth for all levels of local governments.

Due to the delayed impact of the five-year agricultural productivity formula used by Iowa to assess agricultural property, the taxable value of real property in the State can be expected to continue to climb at least through FY 2022 and this should lessen the need for property tax rate increases. However, the changes made in [SF 295](#) by the 2013 General Assembly will result in a lower level of annual statewide taxable value growth than would have otherwise been the case.

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