Political Pressure for Property Tax Relief

TX: Property tax revolt led to 2015 adoption of $10k increase in homestead exemption and super-majority to raise property tax rates

ND: Movement led to 2012 referendum to eliminate property tax (Voted down)

IL, PA: Debates about property tax relief holding up passage of FY16 budgets
Property Taxes and Housing Prices

3 Year Lag After Housing Prices Chg:
- Peak: 2009-2010
- Trough: Late 2014
- Recovery: 2015-2018

Projections (Real Per Capita)
- FY16 = 1.0%, FY17 = 1.5%

Quarterly Summary of State & Local Taxes; FHFA U.S. All Transactions Index; CPI-U; Total Population of U.S. Projections use three year lag and 0.4 elasticity w.r.t. housing price changes.
• Think tank focused on use, regulation, and taxation of **land**

• Work on property tax, urban planning, land conservation, municipal fiscal health

• Property tax matters because it’s the linchpin for local gov’t
1) Strengths and Weaknesses

2) Options for Property Tax Relief

3) How Property Tax Relief Programs Affect State Governments
State + Local Gov’t Taxes in 2012 (Billions)

- **Property Tax**
  - Local: $446 B
  - State: $0 B

- **Sales Tax**
  - Local: $0 B
  - State: $315 B

- **Income Tax**
  - Local: $0 B
  - State: $307 B

Source: U.S. Census Bureau, Census of Government Finances. Income tax is personal income tax; sales tax is general sales tax.
State-Local Taxes as % Family Income

- Property Tax
- Sales & Excise Taxes

### Revenue Changes During Great Recession

(\% \text{Chg. in Real Per Capita State-Local Tax Revenues, Peak to Trough})

<table>
<thead>
<tr>
<th>Tax Type</th>
<th>Revenue Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property Tax</td>
<td>-5.5%</td>
</tr>
<tr>
<td>Sales Tax</td>
<td>-9.2%</td>
</tr>
<tr>
<td>Income Tax</td>
<td>-19.8%</td>
</tr>
</tbody>
</table>

Source: U.S. Census Bureau, Annual Surveys of State and Local Government Finances.
• **Criticisms of property tax:**
  - Property taxes too high
  - Not directly tied to ability to pay
  - Regressive?

• **Strengths of property tax:**
  - More progressive than alternative revenue sources
  - Stable over the business cycle
  - Accountability on gov’t spending and taxes
Outline

1) Strengths and Weaknesses

2) Options for Property Tax Relief

3) How Property Tax Relief Programs Affect State Governments
## Tax Limits

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Property Tax Cut from 1978-1982 (Real Per Capita Taxes)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>% Chg.</td>
<td>53% ↓</td>
<td>35% ↓</td>
</tr>
<tr>
<td>State Rank</td>
<td>3rd to 23rd</td>
<td>2nd to 10th</td>
</tr>
</tbody>
</table>

Source: U.S. Census Bureau, Annual Surveys of State and Local Government Finances.
## Tax Limits

<table>
<thead>
<tr>
<th>Limits apply to</th>
<th>CA Prop. 13 (1978)</th>
<th>MA Prop 2 ½ (1980)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Assessed values of individual properties</td>
<td>Property tax levy for entire municipalities</td>
</tr>
<tr>
<td>Growth rate limit</td>
<td>Lesser of 2% or inflation</td>
<td>2.5% plus taxes on new properties</td>
</tr>
<tr>
<td>Approach</td>
<td>Assessment limit</td>
<td>Levy limit</td>
</tr>
<tr>
<td>Absolute limit</td>
<td>Tax on individual property can’t exceed 1% of it’s value</td>
<td>Tax for entire municipality can’t exceed 2.5% of total value in the municipality</td>
</tr>
</tbody>
</table>
# Tax Limits

## CA Prop. 13 (1978) vs. MA Prop 2 ½ (1980)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Limits apply to</td>
<td>Assessed values of individual properties</td>
<td>Property tax levy for entire municipalities</td>
</tr>
<tr>
<td>Growth rate limit</td>
<td>Lesser of 2% or inflation</td>
<td>2.5% plus taxes on new properties</td>
</tr>
<tr>
<td>Approach</td>
<td>Assessment limit</td>
<td>Levy limit</td>
</tr>
<tr>
<td>Property tax based on market values?</td>
<td>No</td>
<td>Yes</td>
</tr>
</tbody>
</table>

## Consequences of severing link between property values and taxes:
- Horizontal inequities
- Lock-in (Mis-sized homes; Don’t move for jobs)
Homestead Exemptions

- Exempt certain amount of assessed value from taxation → Reduces amount of taxes owed on property

<table>
<thead>
<tr>
<th></th>
<th>$100,000 Home</th>
<th>$200,000 Home</th>
<th>$400,000 Home</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax before exemptions (1% rate)</td>
<td>1,000</td>
<td>2,000</td>
<td>4,000</td>
</tr>
<tr>
<td>$20,000 Homestead Exemption</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxable value after $20,000 exemption</td>
<td>80,000</td>
<td>180,000</td>
<td>380,000</td>
</tr>
<tr>
<td>Tax after $20,000 exemption</td>
<td>800</td>
<td>1,800</td>
<td>3,800</td>
</tr>
<tr>
<td>$ Savings</td>
<td>200</td>
<td>200</td>
<td>200</td>
</tr>
<tr>
<td>% Savings</td>
<td>20%</td>
<td>10%</td>
<td>5%</td>
</tr>
</tbody>
</table>
Homestead Exemptions

- Exempt certain amount of assessed value from taxation → Reduces amount of taxes owed on property

- **Percentage** exemptions (i.e. 10%) not very progressive compared to **fixed dollar** exemptions (i.e. $10k)

- **Broad based programs:**
  - All owner-occupied primary residences (25 states)
  - All senior homeowners (7 states)
  - Businesses, renters, second homes not eligible → Shift tax burden towards these properties
Circuit Breakers

• Circuit breakers prevent households from being overburdened by property taxes

• **Targeted** rather than broad-based
  • Focuses on households with heaviest tax burdens
  • Seniors on fixed incomes; People who lost their job
  • Cost-effective approach

• “Classic” approach sets a **threshold** percentage of income that property taxes must exceed before any tax relief is available
  ➔ Circuit breaker benefit offsets taxes above this point
5% Threshold Circuit Breaker

Property Tax as % Income

Circuit breaker kicks in above 5%

Circuit breaker credit

Property Tax Due
Outline

1) Strengths and Weaknesses

2) Options for Property Tax Relief

3) How Property Tax Relief Programs Affect State Governments
Property Tax Relief Funded by State Gov’t

- Circuit breakers and half of homestead exemption programs are state-funded
  - Income tax credit, Rebate check
  - Property tax credit with state reimbursement

- Arguments for state funding
  - Mitigates disparities in property wealth across communities
  - State funding ≈ Property Tax Cut; Local Funding ≈ Tax Shift
    - Locally funded exemptions: Tax base ↓ → Tax rates ↑
      → Businesses and others pay more
  - But: May incentivize higher local spending → Property tax cut ↓
Property Tax Limits Impact State Budgets

• Property tax limits don’t *reduce* local gov’t spending; they *shift* revenue composition

• Revenue shift can impact state governments
  • **State aid**: Largest local revenue source
  • **Local sales/income taxes**: Shared tax base
    – Higher **total** tax rates (State + Local)
Conclusion

• Strengths and weaknesses
  • **Strengths:** Stable revenue source, promotes accountability, progressive compared to sales tax and charges/fees
  • **Weaknesses:** Not directly tied to ability to pay, large tax burden

• Options for reforming property tax
  • **Assessment limits (CA Prop 13):** Horizontal inequities; lock-in
  • **Levy Limits (MA Prop 2 ½):** Better approach for tax limit
  • **Homestead exemption:** Broad-based; makes tax more progressive
  • **Circuit breakers:** Targeted relief to most burdened households

• Property tax relief normally affects state government
  • Property tax relief programs often state-funded
  • Tax limits: State aid ↑, Shared tax base
Contact Information

Adam H. Langley
Senior Research Analyst
Lincoln Institute of Land Policy
617-503-2117
ALangley@lincolnininst.edu