Appraisal Reform: Think Outside the Box

By John Merrifield,
Professor of Economics
Director, Entrepreneurial Conservatism Institute
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End it, don't mend it. Mostly, thanks to California, Oregon, and to a lesser extent, Florida, we have empirical evidence that even they over-estimated the benefits of reassessing property value between the times when a home sells. You see, those states, like almost everyone else, assumed that ending reassessment would reduce property tax revenue, but they ended it anyway because of periodic re-appraisal's (PR) significant disadvantages. California and Oregon ended PR, despite the expected fiscal impact, because local governments refused to offset the effect of rising property values with lower property tax rates. The resulting rapid increase in property taxes was forcing some people to sell their homes, while others made painful spending cuts in order to pay the higher taxes.

My preliminary findings from an analysis of data from 31 states indicates that PR has no long run fiscal benefits, and the short-run benefits are dubious even in fast-growing places like California, Florida, and Oregon. The reasons are intuitive. While PR can keep the taxable value of fast-appreciating property closer to market value (catch up effect), PR reduces market value (market value effect). The market value effect results from the renovation deterrent of increased taxation, and because the possibility of appreciation-induced, much increased property taxation reduces what people will pay for a residence. Renovation deterrence reduces market values in entire neighborhoods. Among the 31 states, the catch-up effect offsets the market value effect. The market value effects are strongest in states like Texas that have the highest property tax rates. Indeed, there is some preliminary evidence that Texas' ten percent per year limit on assessment growth increases property values more than enough to offset the effect of reduced 'catch up' on rapidly appreciating properties.

Students of California's Proposition 13 and Oregon's Measure 50 will note that those states' property tax revenues did shrink a lot. My empirical analysis says that the termination of PR was not the reason for reduced property tax revenues. Revenues fell because both states rolled back assessments. For example, Oregon set each property's 1998 assessment at ninety percent of the 1996 assessment. California reduced the property tax rate from a statewide average of about 2.5 percent to a maximum of one percent. Because of rapid property turnover, taxable property value (acquisition value adjusted for inflation) in both states grew rapidly.

The remaining argument for PR is that it is necessary to pursue equal taxation of properties of equal value. In a neighborhood where homes appreciate must faster than the rate of inflation, new residents will owe more taxes than longtime residents in similar homes. PR is not needed to correct that inequity, and it is not clear that an inequity that mostly favors infrequent movers, especially the poor, should be corrected by any

means. The U.S. and California Supreme Courts have ruled that acquisition value is a legal basis for assessed value despite such inequities. Market value of property is a poor measure of ability to pay taxes, or the value of benefits received from local governments. If the political process demands pursuit of equal taxation of properties of equal value, that can be achieved with deferral of taxes on property appreciation in excess of the overall rate of inflation until the time the property is sold.

The Governor's Task Force on Appraisal Reform will present their report to Governor Perry later this month. Contact them with your thoughts on this important matter through: annerben@flash.net. For a copy of my November 10 testimony, e-mail me at: jm1eci@sbcglobal.net