Lynn Swann would Simplify Property Tax and Limit its Growth

by Howard Richman and Raymond Richman

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Lynn Swann, the former Pittsburgh Steeler wide receiver famous for acrobatic catches, is now running for Governor of PA on a tax reform platform. His property tax proposal is especially attractive to homeschoolers. It not only simplifies the tax, greatly reducing the costs of administration both to the government and home owner, but it also limits future property tax growth.

Predictably, the teachers unions are opposing this proposal. They realize that it would prevent school districts from continuing to raise property taxes at a rate much faster than inflation. Every other industry, but education, has cut costs in the wake of the computer revolution. Swann's proposal would force school districts to reduce their staffs as their enrollment declines if the trend toward less-expensive and more efficient cyber-charter schools continues.

Swann's proposal is actually quite simple. When people buy homes, the assessment is the purchase price. After that, the assessment does not go up and your property tax cannot go up faster than the rate of inflation. A similar proposal, called Proposition 13, was passed in California as a result of a voter referendum. Prop. 13 limited the maximum rate of tax to 1% of market value, excluding pre-existing indebtedness, and limited the increase of assessed valuations to no more than 2% per year. Properties newly sold were to be assessed at their sales prices. Like Prop. 13, Swann's proposal overcomes three drawbacks that cause the real estate tax to be held in bad repute:

1. *Unfair assessments*. Home owners in some counties have to spend much time appealing their assessments. Those who don't appeal sometimes pay unfair tax rates.
2. *Tax Hikes*. Counties and school districts take advantage of rising property values and assessments to raise your taxes without appearing to do so.
3. *Uncertainty*. Without Swann's proposal, you never know how much tax you will pay in the future. Sometimes people have to sell their homes just because they can't afford the rising taxes.

There is also a great increase in efficiency. Fewer assessors are required to administer the tax. There is no need to reassess properties annually. Only newly sold properties require assessment and their assessment is their sales prices. Properties undergoing major reconstruction also need to be reassessed but the cost of the remodeling is simply added to the existing assessment. There are problems of fairness when properties are damaged by earthquakes, fires, and the like or transferred involuntarily as a result of eminent domain, for example. And assessors will still be needed to determine the fair market value when property is transferred with payments in kind in place of cash, etc. In California, the number of assessors declined from 2100 in 1977-78 to 1,550 in 1986-87.

Moreover, Prop. 13 appears to have had no negative economic effects and it appears not to have impeded purchases of existing or new houses. The California real estate market has continued to be the strongest in the nation. Indeed, it could be argued that Prop. 13 has encouraged home ownership because it eliminated the uncertainty of what future taxes would be.

The major criticism of Prop. 13 was that over time it would cause substantial differences in the taxes paid by owners of comparable properties. The longer one owns a property the lower will be the ratio of assessed value to market value compared to more recently sold properties. While this is true it does not necessarily mean inequitable differences in the tax burdens of old and new property owners. The reason for this is the fact that land-owners bear the entire burden of real estate taxes by a process that economists call backward shifting. As a result of this process buyers of properties pay less than they would if comparable properties were similarly assessed, and sellers receive less. To illustrate how this works, take the case of two identical homes, one purchased years ago and now assessed at $200,000 paying a tax of $4,000 per year and the other just purchased for $300,000 and liable to a tax of $6,000 per year. What this economic argument says is that the buyer of the new home would have been willing to pay $320,000 if his tax were just $4,000, the difference, $20,000, being the capitalized value of $2,000, his higher tax liability. The seller will receive $300,000 whereas in the absence of the tax differential he would have received $320,000.

Governor Rendell has an alternative property tax proposal which only makes property taxes more complicated. He proposes that certain classes of elderly poor property holders can apply for and receive tax rebates. His is just one more welfare system that rewards people for being poor and gives them an incentive against making more income.

Some people advocate eliminating the property tax altogether. This would be a disaster for local governments. No longer would they have their own independent source of revenue. Any other tax that they might levy would chase people out of their districts. Moreover, eliminating the property tax would not make home ownership any less expensive. Since property taxes are backward shifted to the property owner, eliminating the property tax would just make homes more expensive to buy.

The teachers' unions will oppose Swann's property tax proposal because it would make it harder for school districts to rapidly raise property taxes. Those homeschoolers who are home owners or want to become home owners should support it.

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