Limiting the Property Tax Assessments to Slow Gentrification

A recent [New York Times](http://www.nytimes.com/2014/03/04/us/cities-helping-residents-resist-the-new-gentry.html) article on gentrification noted that a number of cities including Boston, Philadelphia and Washington are considering freezing the property assessments of long-time homeowners in gentrifying neighborhoods.

There appear to be two underlying concerns with gentrification. The first expressed, perhaps most recently by [Spike Lee](http://www.nytimes.com/2014/02/27/nyregion/spike-lee-exchange-highlights-gentrification-debate.html?action=click&contentCollection=U.S.&module=RelatedCoverage&region=Marginalia&pgtype=article), is a general aversion to neighborhood change. New residents (with higher income) may cause a shift in the mix of stores and restaurants that displaces the establishments frequented by long-term residents. New residents may also bring new social norms with respect to public conduct, noise, and willingness to report existing coding violations or advocate for greater enforcement. More generally, existing residents may suffer the loss of social capital as friends move away or the look and feel of neighborhood changes.

A second, distinct concern is that while both new and existing residents may value the increased retail amenities and engaged neighbors, they can’t afford to stay and enjoy improved neighborhood quality because rising rents and property taxes make it too costly to stay.

To help existing homeowners stay in their neighborhoods, some cities are planning to cap property assessments. While the desire to protect existing residents from gentrification appears to be new, assessments caps have been around since California’s [Proposition 13](http://en.wikipedia.org/wiki/California_Proposition_13_%281978%29) in 1978. After California, 11 additional states passed laws capping individual property assessment caps.

Ideally, we could observe the duration of time that existing residents remain in their home in the face of gentrification. However, there are few individual level datasets with the fine geography to allow such an analysis. As an alternative, we can look at the pace of gentrification across states to see whether poor neighborhoods in states with assessments caps gentrify slower. Table 1 presents the number and share of census tracts in the central city that gentrified between 2000 and 2007. that passed an assessment cap between 1978 and 2001. We rely on the table of assessment caps compiled by [Haveman and Sexton](http://www.taad.org/Property%20Tax%20Assessment%20Limits--Lessons%20from%2030%20Years%20of%20Experience.pdf) that identifies ten states plus the city of New York that limits the growth of assessed to inflation or a maximum percentage rate that ranges from 2% (California) to 10% (Texas). I rely on the dataset of gentrifying neighborhoods compiled by my colleague [Dan Hartley](http://www.clevelandfed.org/research/trends/2013/1113/01regeco.cfm) at the Cleveland Fed. Specifically, I look at the proportion of neighborhoods in the central city where the median house price changed from below the median MSA house price to above the median house price between 2000 and 2007. Using that definition, almost 20 percent of low income tracts in central cities gentrified, compared to 15 percent in cities without assessment caps. While hardly definitive, this suggests that assessment caps are not, in and of themselves sufficient to prevent gentrification.

Table 1. Share of Neighborhoods that Gentrified Between 2000 and 2007 with and without statutory caps on the growth in assessed value

|  |  |  |  |
| --- | --- | --- | --- |
| Neighborhood Type | Low Priced Neighborhoods in 2000 | Gentrified Between 2000 and 2007 | Share |
| Assessment Cap | 3,513 | 689 | 0.196 |
| No Assessment Cap | 3,296 | 489 | 0.148 |
| Difference |  |  | 0.478\* |

\*Statistically different from zero at all standard cut-offs.

One reason that policy makers shouldn’t be deterred based solely on Table 1 is that states may have passed assessment caps in response to rising home prices. That was certainly one of the factors behind Prop-13. So a state experiencing persistent house price growth might experience greater gentrification pressure and also impose assessment caps that may confound the mitigating effect of the cap. However, if voter wish to limit the growth in property taxes they don’t need to cap assessments, they can just restrict the growth in property tax revenue. At the same time, assessment caps that don’t also cap the property tax rate don’t actual constrain taxes, but instead [shift the tax burden from longtime owners to new buyers](http://ideas.repec.org/p/fip/fedawp/2009-19.html). In Table 2 we limit the sample to states that have a binding revenue growth cap or a cap on assessments and municipal tax rates. We rely on the work by [Hoyt, Coomes and Biehl (2011)](http://onlinelibrary.wiley.com/doi/10.1111/j.1540-6229.2010.00288.x/abstract) that identifies state limits on property tax revenue growth and municipal tax rates.

Table 2. Share of Neighborhoods that Gentrified Between 2000 and 2007 with some form of Binding Property Tax Limit

|  |  |  |  |
| --- | --- | --- | --- |
| Neighborhood Type | Low Priced Neighborhoods in 2000 | Gentrified Between 2000 and 2007 | Share |
| Assessment Cap | 2,392 | 504 | 0.21 |
| No Assessment Cap | 1,792 | 305 | 0.17 |
| Difference |  |  | 0.041\* |

\*Statistically different from zero at all standard cut-offs.

So even when we limit the sample to states that have chosen to constrain the property tax in some way we still observe assessment caps seeming to accelerate gentrification rather than slow it. How can that be? One possibility is that because these are state-wide limits the caps have reduced the turn-over in more desirable neighborhoods driving buyers to buy in marginal central city neighborhoods. In that case, targeted assessment caps that only apply to currently low-priced neighborhoods may be more efficacious. On other hand, the existence of an assessment cap may increase the long-run return from “pioneering” in a low-priced neighborhood. In any case, there seems to be little evidence that rising property taxes speed gentrification.

What we observe is that