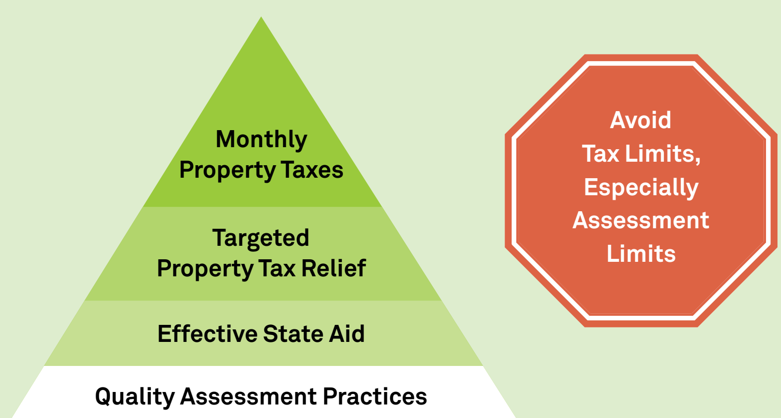
PROPERTY TAX RELIEF FOR HOMEOWNERS

By Adam H. Langley and Joan Youngman

The property tax is uniquely suited for supporting the independent local governments that play a critical role in the United States federal system. Localities fund a variety of key public services that enhance quality of life for their residents, including K–12 education, public safety, parks, infrastructure, and much more. Local governments—which include cities, counties, school districts, and all other jurisdictions below the state level—are the closest to the people and most trusted by them. An important reason for this is the proximity and flexibility that allow local governments to understand and respond to the needs of residents. But independent decision making requires that local governments have the ability to raise sufficient revenues to fund their operations.

The property tax has important strengths as a local revenue source. Its immobile tax base allows localities to assemble a package of taxes and services reflecting the preferences of their citizens. It provides stable revenue over the business cycle, promotes transparency regarding fiscal decisions, and tends to impose less drag on the economy than other taxes. The property tax is also progressive compared to most alternatives; that is, it tends to take a relatively smaller share of income as incomes fall—especially when targeted tax relief options such as circuit breakers and homestead exemptions are in place.

The Keys to an Equitable and Efficient Property Tax System



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These strengths lead to heavy local reliance on property taxes. The property tax accounts for nearly half of all revenue raised by local governments in the United States. Local governments raise over five times more revenue from property taxes than from sales taxes, and over 10 times more than from income taxes.

Like any tax, however, the property tax faces challenges. Fiscal disparities across communities are a problem for any local tax and mean that poorer jurisdictions may struggle to provide adequate services at reasonable tax rates. Since it does not consider current income, the property tax can be unaffordable for those who are house-rich but cash-poor. In addition, property taxes can potentially increase sharply from one year to the next, they may be based on inaccurate or outdated estimates of value, and they often must be paid in large lump sums.

The good news is that there are policy options that can effectively address all of these challenges. When used together, they can lead to a tax system that is fair and affordable while still providing the revenue needed to support quality public services. But it is important to design relief programs carefully to address specific issues, because untargeted policies can cause excessive revenue losses and serious unintended consequences.

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Designing Targeted and Effective Tax Relief Policies

Research shows that most property tax revolts are a response to dramatic increases in property taxes, particularly when these result from rising home values. These political reactions have often led to some form of state-level property tax limitations, including rate limits, assessment limits, and levy limits. These limits can constrain growth in property taxes, but they may also shift the revenue mix to less reliable sources, reduce the quality of local services, and impede local governments' ability to respond to local preferences and changing circumstances.

To avoid politically unacceptable tax increases without resorting to inflexible tax limitations, it is critical that local officials reduce tax rates during periods of rapid growth in property values. Responsive rate setting, quality assessment practices, and regular revaluations are the foundation of a fair property tax system.

Targeted tax relief policies can build upon that foundation. Circuit breakers, deferrals, and homestead credits each address specific property tax challenges without undermining the strengths of this essential revenue source. Relief programs can make the property tax more progressive, offset rapid tax increases, assist homeowners who face liquidity issues, and help those who are least able to pay.

Homestead Exemptions and Credits

Homestead exemptions and credits are the most common type of property tax relief. These exemptions and credits are usually available for all owner-occupied primary residences, although some states restrict eligibility to seniors or provide seniors with additional benefits. Most jurisdictions exempt a fixed *dollar* amount from taxation, making the property tax distribution more progressive. For example, a $20,000 exemption reduces property taxes by 20 percent on a $100,000 home, 10 percent on a $200,000 home, and 5 percent on a $400,000 home. Some jurisdictions exempt a fixed *percentage* of value from taxation, leaving the property tax distribution unaffected and providing the largest dollar savings to owners of high-value homes. Homestead credits are similar to exemptions, but they reduce tax bills directly rather than reducing taxable values.

Income-Based Homestead Credits

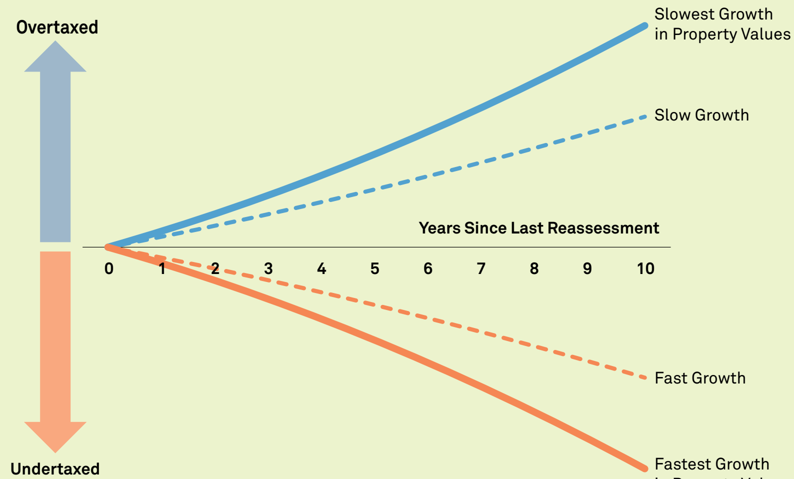
Income-based homestead credits tie the amount of property tax relief to applicants' incomes, with credits decreasing as income increases. These means-tested programs provide more targeted and cost-effective relief than homestead exemptions or credits that do not take income into account. However, means testing can also reduce participation rates and increase administrative burdens.

Quality Assessment Practices Are Essential for Tax Fairness

Accurate assessments are essential for equity under a market-value property tax system. Without them, the distribution of property taxes becomes unfair and arbitrary. Assessment accuracy depends on regular revaluations, and it is enhanced by modern valuation techniques, state oversight of local assessing offices, and effective appeals systems.

The most common cause of inaccurate assessments is that too much time has passed since the last revaluation. The longer a jurisdiction goes without reassessing property values, the greater the tax inequities. Properties with the slowest growth in values (or largest declines) become increasingly overtaxed. Properties with the fastest growth become increasingly undertaxed.

Tax Inequities Grow Without Reassessment



In Colorado, the property tax deferral option for senior homeowners has many elements of a well-designed program, imposing no income ceiling and using a low interest rate on deferred taxes equal to the latest 10-year Treasury note. Taxpayers must submit an annual application to qualify, and the state government makes payments to each county on behalf of those who have deferred their taxes.

Shoveling snow in Crested Butte, Colorado.
Source: John Terence Turner/Alamy Stock Photo.

Income-based homestead credits define several income brackets, and taxpayers within each bracket receive the same property tax reduction. For example, a state might provide a 75 percent property tax credit for households with incomes up to $10,000, a 50 percent credit for incomes of $10,001 to $20,000, and a 25 percent credit for incomes of $20,001 to $30,000. Some states provide a fixed-dollar credit for taxpayers in each income bracket, again with credits decreasing as incomes rise.

Circuit Breakers

Property tax circuit breakers are meant to prevent homeowners from being overburdened by property taxes, just as an electrical circuit breaker prevents electric current overloads. They offer relief when property taxes exceed a threshold percentage of income. Circuit breakers target property tax relief to homeowners paying the highest share of their income in property taxes, such as seniors on fixed incomes, low-income homeowners in gentrifying neighborhoods, and individuals facing a sudden reduction in earnings. These programs are more cost-effective than those that provide a small amount of tax relief to all homeowners, because they can allow significant assistance to the most heavily burdened households at a lower cost overall.

Most states impose income ceilings to restrict eligibility and benefit limits to constrain the amount of relief provided to any taxpayer. It is important to avoid income ceilings and benefit limits that are too low, to ensure that homeowners receive adequate relief.

Deferrals

Property tax deferral programs allow homeowners to delay payment of their property taxes until ownership of the home is transferred. At that point, the full amount of deferred tax becomes due, typically with interest. Deferrals directly address concerns faced by homeowners with substantial home equity but limited cash flow, allowing them to draw on their home equity to pay current property tax bills. Unlike other forms of tax relief, deferrals impose no long-term cost on other taxpayers. Yet they can also provide very substantial assistance—usually allowing homeowners to defer 100 percent of their tax liability.

Summary of Property Tax Relief Programs

Good	Homestead Exemptions and Credits
Better	Income-Based Homestead Credits
Best	Circuit Breakers Deferrals

Eligibility for deferrals is usually restricted to low-income seniors. Deferrals are an excellent solution for these households, as most seniors own their homes and have considerable home equity. In addition, most seniors prefer to age in place, and deferrals ensure that no eligible homeowner will be forced to move due to property taxes.

Recommendations

Property tax relief must be designed thoughtfully to address specific issues and avoid unintended consequences. The following recommendations promote an equitable and efficient tax system.

IMPLEMENT QUALITY ASSESSMENT PRACTICES WITH REGULAR REVALUATIONS. Accurate assessed values are the foundation of a fair property tax system, and regular revaluations are crucial to maintaining accurate assessments. Without them, taxpayers in areas of slow or declining growth will be overtaxed, subsidizing taxpayers in neighborhoods with the greatest property appreciation. Between full revaluations, assessments can be kept current by statistical adjustments and mass appraisal techniques.[1] Regular revaluations should be paired with tax rate reductions during periods of rising values.

UTILIZE WELL-DESIGNED STATE AID FORMULAS. A frequent criticism of the property tax is that poorer communities with low property values cannot supply adequate public services at affordable tax rates. However, this is not a problem with the property tax, but with local taxation generally. Areas that cannot support quality services with their local tax base require transfers from a higher level of government. State aid is the only way to address fiscal disparities across communities and ensure that all localities have the resources to provide quality services, especially public education. State aid formulas should account for socioeconomic factors that affect expenditure needs and differences in the local costs of providing public services.[2]

PROVIDE TARGETED AND COST-EFFECTIVE PROPERTY TAX RELIEF WITH CIRCUIT BREAKERS AND DEFERRALS. Circuit breakers target relief to households paying the highest share of their income in property taxes. These may include senior citizens on fixed incomes, low-income homeowners in gentrifying neighborhoods, and workers who have lost their jobs. These programs offset taxes above a threshold percentage of income and can provide effective relief to the most heavily burdened households.[3]

Tax deferrals allow homeowners to delay payment of their tax until their home is sold or inherited, at which point the deferred taxes are due, together with any interest. Deferrals provide substantial assistance to homeowners who are cash-poor but house-rich, allowing them to defer 100 percent of their tax liability and draw on their home equity to pay current property tax bills. They are particularly appropriate for senior citizens who wish to age in place.[4]

ALLOW HOMEOWNERS TO PAY PROPERTY TAXES ON A MONTHLY BASIS. Instead of requiring lump-sum payments that can create financial challenges for households and increase tax delinquency, local governments should consider alternative payment plans. This is typically done through prepayment programs that allow monthly payments to accumulate in an escrow account, which is used to pay the annual or biannual tax bill.[5]

AVOID TAX LIMITATIONS, ESPECIALLY ASSESSMENT LIMITS. Tax limits are one of the most common responses to political pressure for property tax relief, but they are generally a poor choice.[6] They are untargeted and impose a one-size-fits-all constraint on very different local governments. Limits on growth in assessed values are particularly harmful. They create unpredictable winners and losers, shift the tax burden from owners of rapidly appreciating property to those whose home values are growing slowly or even depreciating, and generate large inequities where owners of homes of similar value face very different tax bills.[7] Rather than imposing inflexible tax limits, state and local governments should provide targeted tax relief that preserves the revenue needed to maintain quality public services.

This Policy Brief is based on *Property Tax Relief for Homeowners*, a Policy Focus Report by Adam H. Langley and Joan Youngman (Cambridge, MA: Lincoln Institute of Land Policy, 2021).

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3 John H. Bowman, Daphne A. Kenyon, Adam Langley, and Bethany P. Paquin. 2009. *Property Tax Circuit Breakers: Fair and Cost-Effective Relief for Taxpayers*. Policy Focus Report. Cambridge, MA: Lincoln Institute of Land Policy.

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6 Joan Youngman. 2016. "Tax Restrictions and Assessment Limits." In *A Good Tax: Legal and Policy Issues for the Property Tax in the United States*. Cambridge, MA: Lincoln Institute of Land Policy.

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