Assessment Limits: Could We Live with the Consequences?

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Property tax – the most unpopular tax?

- It is a visible tax
  - Lump sum payments not deducted at source
  - Visible services
  - Visibility increases taxpayer scrutiny
- It can be a volatile tax
  - Market value can be volatile, not stable and predictable
  - If assessed value increase is greater than average of municipality, taxes will go up (and vice versa)

Assessment Limits

- Visibility and volatility have led to assessment limits in many US states and pressure to impose limits in Canada
- What has been the experience in the US?
- Could we live with the consequences in Ontario?

Outline of Presentation

- What was the impact of Proposition 13 in California?
- What would be the impact in Ontario?
- What's wrong with assessment limits?
- Are there other ways to address volatility?

Proposition 13 in California: How does it work?

- Time of sale reassessment: assessment increased by the lesser of inflation or 2% per year until property is sold

- No reassessment if property transferred to children of owner

- Seniors (over 55) can transfer assessed value to a replacement dwelling of equal or lesser value without reassessment

Impact of Proposition 13 in California

- Inequities: some owners pay much more in taxes than neighbours in comparable properties

- Inequities can go on for generations: one young family buys a new home and pays market value taxes; another inherits a home and pays taxes on parents’ acquisition value

Impact of Proposition 13 in California

- Proposition 13 favours older, more affluent generation over younger first-time homebuyers

- Young first-time homeowners face higher taxes because starter homes are reassessed more frequently

- Decreases household mobility

Impact of Capping until Time of Sale in Ontario: Simulations

- What would be the impact on property taxes today if we had introduced a time of sale reassessment in Ontario in 1980?
- What if we capped assessments at 5%, 10%, or the CPI until time of sale?
- Who wins? Who loses?

Simulations

- Market value is estimated for each residential property using sale prices (where valid and available) or market factors based on sale prices in the neighbourhood going back to 1980
- Approximately 3.6 million residential properties
- Market value adjusted for renovations
- Adjust acquisition value by capped amount (5% or 10% or CPI) until time of sale
- Look at changes in assessed value by property value, income group, age of owner, property type

Figure 1: Impact of 5% Capping by Property Value

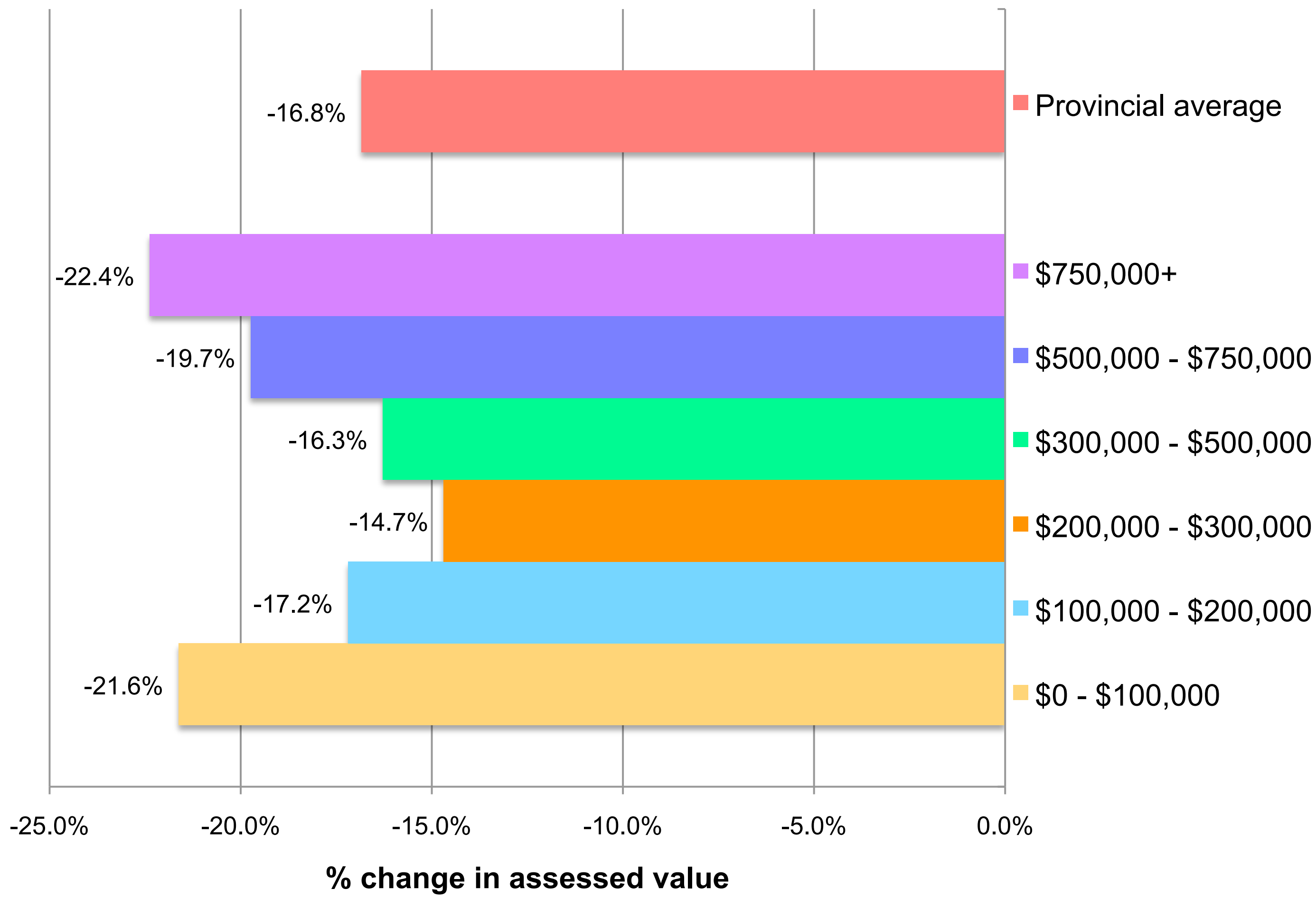


Figure 2: Impact of 5% Capping by Income Group

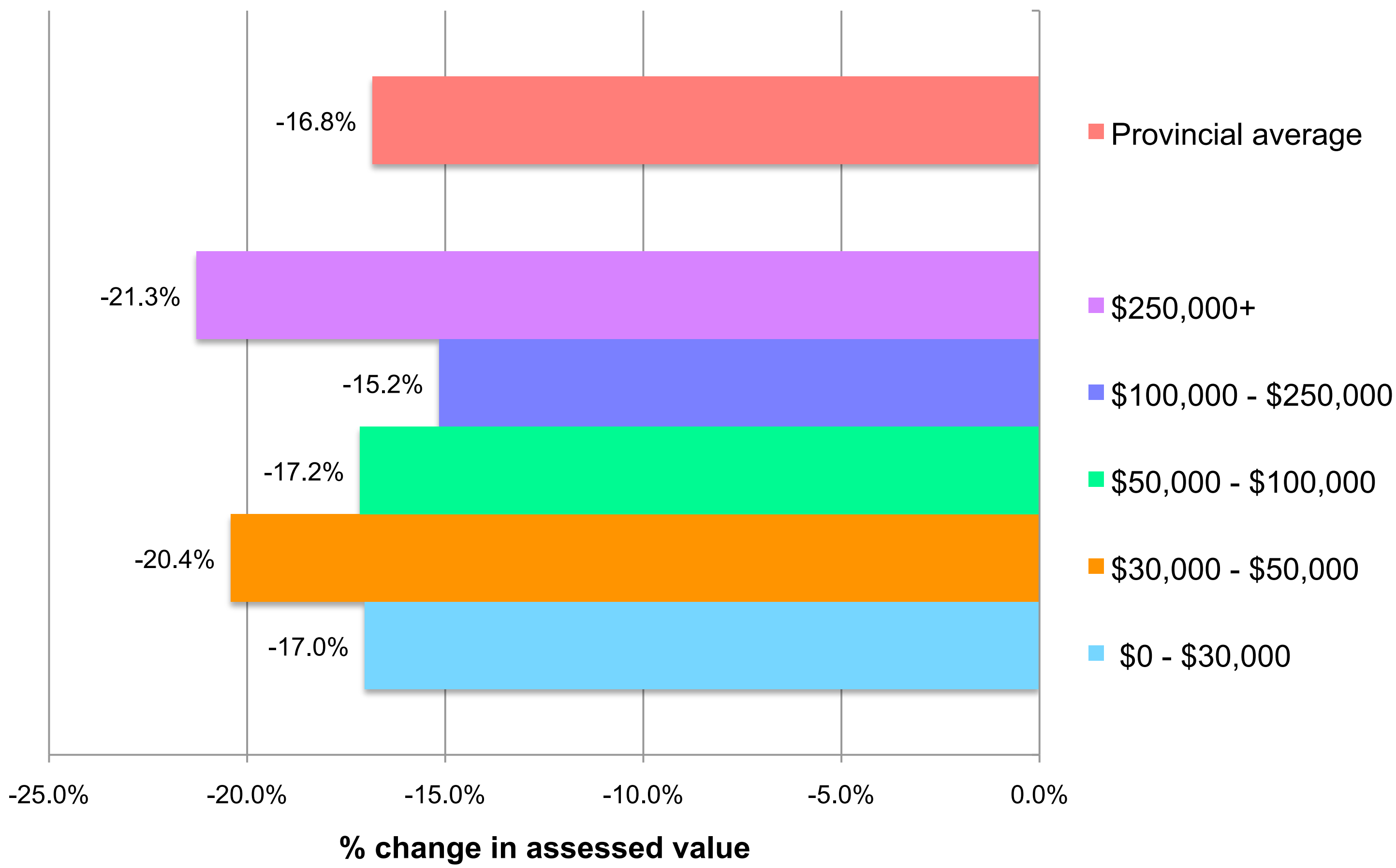
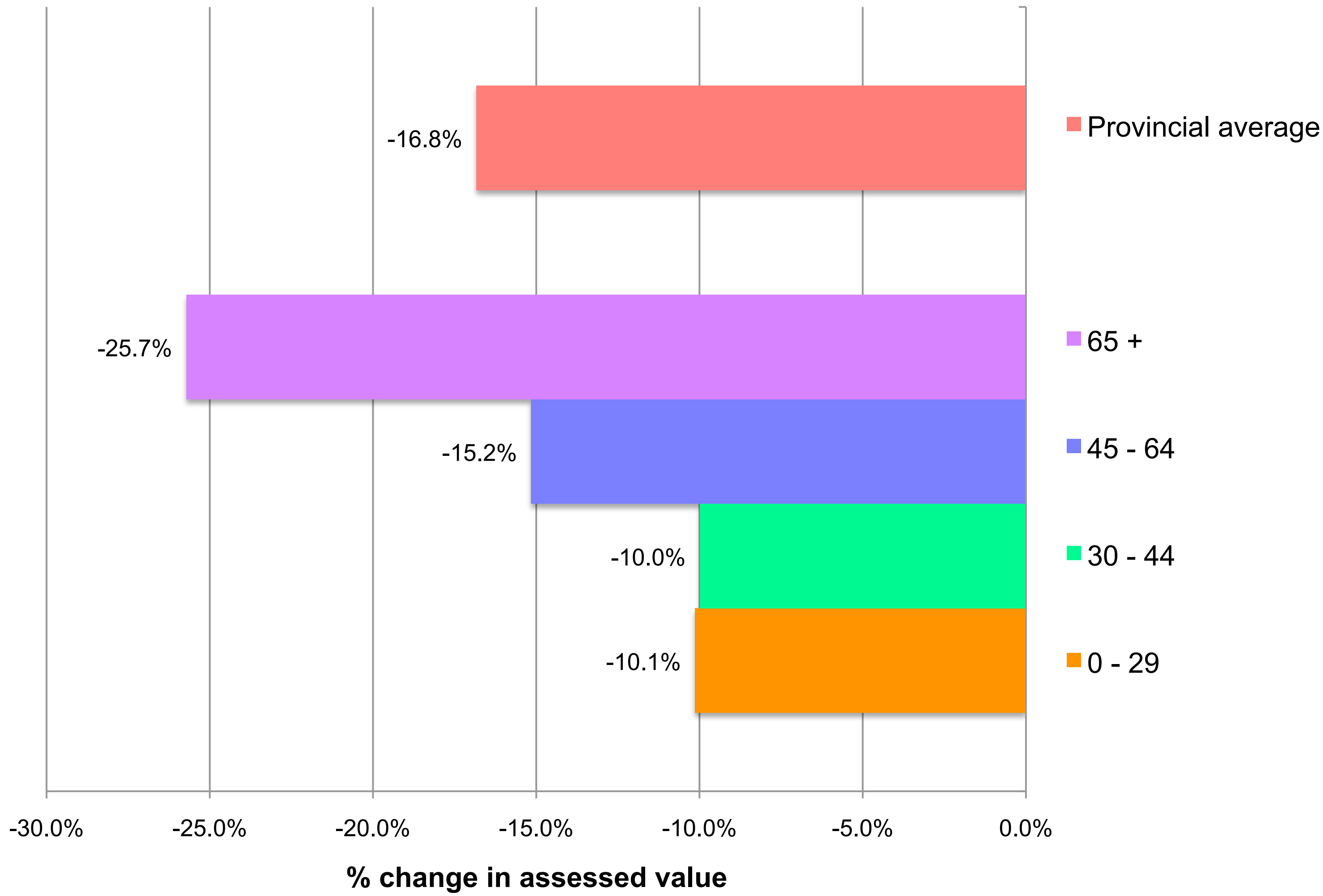


Figure 3: Impact of 5% Capping by Owners' Age



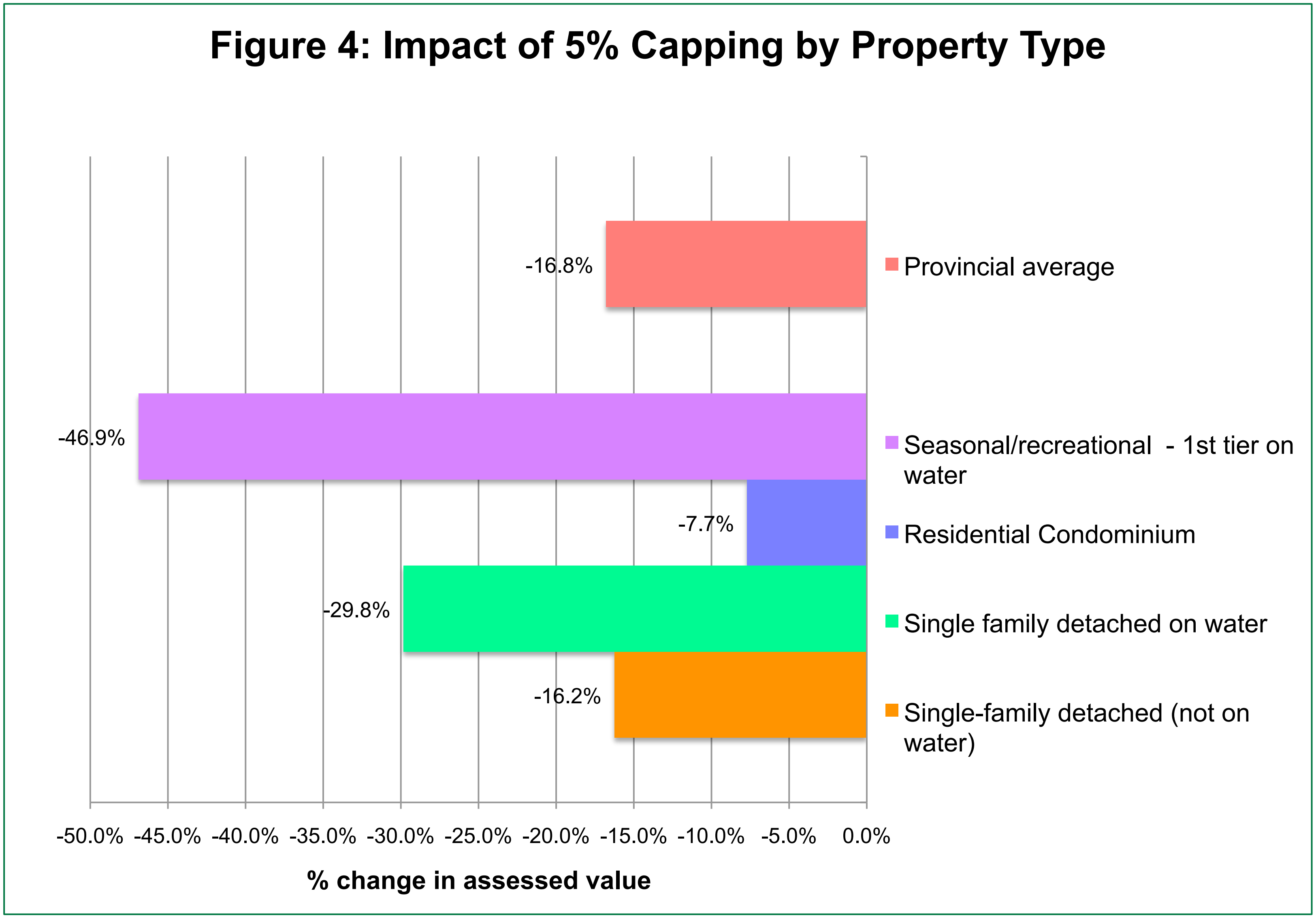


Figure 4: Impact of 5% Capping by Property Type
-16.8%
-46.9%
-7.7%
-29.8%
-16.2%
Provincial average
Seasonal/recreational - 1st tier on water
Residential Condominium
Single family detached on water
Single-family detached (not on water)
-50.0% -45.0% -40.0% -35.0% -30.0% -25.0% -20.0% -15.0% -10.0% -5.0% 0.0%
% change in assessed value

Potential Impact of Capping in Ontario

- Capping favours high and low-valued properties at the expense of medium-valued properties (majority of properties)
- Capping favours high-income owners and low-income owners at expense of middle income owners (majority of owners)
- Capping favours elderly homeowners at expense of young homeowners
- Capping favours properties increasing in value rapidly (e.g. waterfront, seasonal) at expense of other properties

What is the impact of capping on taxes?

- Consider 3 properties of equal value in the City of Toronto that sold in three different years (1985, 1995, 2005)
- Assume tax rate increases to compensate for decrease in assessment – revenue neutral
- Compare property taxes in 2008 with and without capping

Impact of 5% Capping on Three Properties Sold in Different Years

	Date sold	2005 CVA for 2008 taxation	2008 Property taxes	5% capped CVA	2008 property taxes with capping	Impact on property taxes
Property A	1985	400,000	3,499.69	321,000	3,484.03	(15.67)
Property B	1995	400,000	3,499.69	337,000	3,657.68	157.99
Property C	2005	400,000	3,499.69	400,000	4,341.46	841.77
Total		1,200,000	10,499.07	1,058,000	11,483.17	984.10
Tax rate			0.874923%		1.085366%*	
* Tax rate reflects revenue neutral tax rate for the whole city.						

Impact of 10% Capping on Three Properties Sold in Different Years

	Date sold	2005 CVA for 2008 taxation	2008 Property taxes	10% capped CVA	2008 property taxes with capping	Impact on property taxes
Property A	1985	400,000	3,499.69	400,000	3,528.20	28.51
Property B	1995	400,000	3,499.69	400,000	3,528.20	28.51
Property C	2005	400,000	3,499.69	400,000	3,528.20	28.51
Total		1,200,000	10,499.07	1,200,000	10,584.61	85.54
Tax rate			0.874923%		0.8820509%*	

* Tax rate reflects revenue neutral tax rate for the whole city.

Impact of Capping at CPI on Three Properties Sold in Different Years

	Date sold	2005 CVA for 2008 taxation	2008 Property taxes	CPI capped CVA	2008 property taxes with capping	Impact on property taxes
Property A	1985	400,000	3,499.69	209,000	2,665,35	(834.35)
Property B	1995	400,000	3,499.69	260,000	3,315.74	(183.95)
Property C	2005	400,000	3,499.69	400,000	5,101.14	1,601.45
Total		1,200,000	10,499.07	869,000	11,082.22	583.15
Tax rate			0.874923%		1.2752848%*	

* Tax rate reflects revenue neutral tax rate for the whole city.

Impact of Capping

- Benefits houses that sold a long time ago at the expense of houses that sold recently
- The higher the capping limit, the less the distortions
- Taxes can actually increase for some properties whose assessments went down!

What are the Problems with Assessment Limits?

- Breaks link between taxes and market values:
  - Taxes less uniform and more arbitrary
  - Properties with similar values pay different taxes
  - Erodes the tax base
  - No incentive to review assessment (since it is not used for taxes; never correct assessment errors)
  - Those with capped assessments have incentive to demand more expenditures

What are the Problems with Assessment Limits?

- Assessment caps take pity on those who are being made wealthier by the market at the expense of those whose property values are stagnant

- Stability and predictability at the expense of equity

- But, ignoring sound economics principles can result in an even less equitable tax in the long run and even greater taxpayer resistance

Problems with Assessment Limits: What Are Others Saying?

- “Phantom” tax relief – the appearance of property tax relief where none actually exists
  - Mark Haveman, Minnesota Taxpayers Association
- “Once a freeze is imposed, the process of thawing may be too painful to bear”
  - Joan Youngman, Lincoln Institute of Land Policy

Are there other ways to address volatility?

- Existing tools can be used to mitigate impact of tax increases:
    - Property tax credits for low-income taxpayers
    - Tax deferrals for the elderly (to address cash-flow problem)
    - Phase-ins of tax increases
    - Unduly burdensome provision under Section 365 of the Municipal Act (for those facing undue hardship)

Are there other ways to address volatility?

- Accuracy in assessment is critical to a market value assessment base
- Assessment increases cannot be used as excuse for property tax increases
  - truth in taxation
  - revenue neutrality
- Taxpayer (and media) education is needed to understand the relationship between assessment and taxes

Addressing Volatility

- Taxpayers could be offered different payment options
- Need to address real hardships
- Don’t tamper with assessment base; mitigate impact of increases on those who cannot afford them

Concluding Comments

- Current value may have its problems but efforts to cure problems may have unintended consequences

- Need to mitigate tax increases on those who can't afford them (property tax credits, tax deferrals)

- Perhaps the property tax is being used to finance too many services – may need to reduce reliance on the property tax