Property Tax Policy Responses to Rapidly Rising Home Values: District of Columbia, Maryland, and Virginia

Abstract - After presenting information on the level and role of property taxation in the District of Columbia, Maryland, and Virginia, possible policies for rising property taxes due to rapidly rising home values are identified and briefly evaluated. Next, specific property tax relief measures in the District of Columbia, Maryland, and Virginia—including Washington suburbs' local-option measures—are described. The effectiveness of the approaches in dealing with rising home values and their implications for property tax equity are considered. The appropriateness of relief for all homeowners experiencing rapid increases in home values is questioned and alternatives are suggested.

INTRODUCTION

In recent years, housing values have risen rapidly in many areas. Typically, high rates of increase have not been sustained over a long period of time. Nonetheless, rapid increases in value—when translated into higher assessed values—create concerns among homeowners and, therefore, among politicians. In addition, the residential share of the property tax base has risen over time, and recent market patterns have added to this trend (Anderson, Giertz, and McGuire, 2006; Haveman, 2005; Maryland Department of Assessments and Taxation, 2005). In response, many states and localities in recent years have adopted new homeowner property tax relief measures and/or liberalized existing measures; still others have considered additional property tax relief.

This paper looks at homeowner property tax relief measures in the District of Columbia, Maryland, and Virginia, with some emphasis for the two states on measures in their Washington suburbs. The first section below sketches the level and role of property taxation in the three subject jurisdictions.

1 In a 30-year series from 1976 through the first quarter of 2006, the U.S. housing price index reported by the Office of Federal Housing Enterprise Oversight (OFHEO) shows only two periods of double-digit price inflation: 1977–3 through 1979–4 (ten quarters) and 2004–3 through 2006–1 (seven quarters so far). Experience differed across the nine Census regions, nearly all of which saw several quarters of negative change in the 30-year period.
Following this is a section that briefly considers the general sorts of property tax policy responses that might be made to rising home values. The next section describes property tax relief programs in the District of Columbia, Maryland, and Virginia. The concluding section includes discussion of some of the implications of various programs.

PROPERTY TAXATION IN THE DISTRICT OF COLUMBIA, MARYLAND, AND VIRGINIA

Nationwide, property taxation is the major source of local government tax revenue. Virginia comes close to the national average property tax share of local taxes (71.6 percent and 72.9 percent, respectively, in 2002), but Maryland and the District of Columbia do not (56.8 percent and 24.9 percent, respectively). In Virginia, an above–average share of property tax yield is from personal property, particularly motor vehicles. The District, with no overlying state government, has a tax structure more like a state structure than a local one. For this reason, and because the division of fiscal responsibilities between the state and local levels varies across states, it is important to consider the state and local levels together.

In 2002, property taxes were 30.8 percent of combined state and local taxes nationwide, 30.3 percent in Virginia, 27.2 percent in Maryland, and 24.9 percent in the District of Columbia. These figures were up somewhat from 1997 both nationally and in Maryland, but down somewhat in the District and Virginia. These figures were up somewhat from 1997 both nationally and in Maryland, but down somewhat in the District and Virginia. Considering the longer period 1992–2002, the property tax share of all state–local taxes was down slightly nationwide, in Maryland, and in Virginia, but down sharply in the District (drop from 37.5 percent in 1992 to 24.9 percent in 2002).

Property taxes per capita in 2002 were well above the $992 national average in the District of Columbia ($1,405), somewhat above average in Maryland ($1,022), and somewhat below average in Virginia ($948). Relating property taxes to personal income provides a little different picture of relative property tax levels; all three subject jurisdictions are below the 3.22 percent national average (3.06 in the District, 2.80 percent in Maryland, and 2.87 percent in Virginia), reflecting their above–average income levels.

POSSIBLE RESPONSES TO ESCALATING HOME VALUES

Rising assessed values often are unpopular, but what problem is created? Views on this and policy responses differ. Possible responses to a run–up in home values are many. The extremes are doing nothing and providing broad, generous relief to all homeowners. In between are various sorts of targeted relief. In general, the actions taken (if any) will depend upon several considerations, including, but not necessarily restricted to, the following:

- The degree to which housing values are rising—Larger percentage increases in value are more likely to generate a policy response than smaller increases.
- How widespread large increases in housing values are—A response, at least a statewide response, is more likely if increases are experienced widely within and among localities.
- How long the increases have been occurring and the perception of what is likely—Large increases sustained over several years and/or the expectation of sustained large increases seem more likely to elicit a policy response than large increases not expected to persist.

2 The 2002 Census of Governments provides the most recent data on state–local finance on a state–by–state basis at the time this is being written (U.S. Bureau of the Census, 2002).
• The financial ability of the state and/or local governments to provide property tax relief—New or expanded property tax relief programs are more likely when the economy is strong and government revenue flows are strong and rising.

• The policy objective—Plausible policy objectives are (1) placating the largest number of homeowners, at least to some degree, and (2) providing relief from property taxes that truly are burdensome. These are quite different objectives, and the programs that would be appropriate to one would tend not to be appropriate to the other.

The approaches are discussed briefly below. They vary considerably in how effectively they deal with rising property taxes in the face of rising home values. However logical and “fair” a given approach may seem to its proponents, all approaches present some tradeoffs, but the specific approaches differ in their implications for equity and efficiency.

Property tax policy is the province of the states; inter–local differences arise to the extent that state law and administration permit them. Property tax relief may be provided on a uniform basis throughout a state or it may be provided at local option within limits set by the state. Statewide relief may be funded by the state or it may be mandated and left to the local governments to absorb in some way. Most of the possible policy responses discussed below may be implemented statewide or at local option, and with or without state funding.

Do Nothing

One possibility is that governments will provide no special property tax relief to deal with rising home values and rising taxes, and perhaps no property tax relief at all. Property tax relief typically is justified by its proponents on the basis of equity, but relief creates inequities. Perhaps most obvious are the differences in effective property tax rates, whether just between the homeowner class and other property owners, or also within the homeowner class. Differences in effective tax rates undermine both equity and the logic of the property tax as a tax on market value. Another equity concern centers on how the relief is paid for. One possibility is increased property tax rates. Increasing property tax rates undercuts the relief attempt and makes the relief measures partly illusory, and it further worsens the situation for property owners not being granted relief. To the extent property tax reliance is reduced, there must be increases in other taxes or non–tax revenue sources and/or lower levels of public service. Revenue sources used to fund property tax relief may be more regressive than the property tax. Similarly, service cuts may affect people more disadvantaged than the homeowners receiving property tax relief.

Lower effective property tax rates for homeowners also raise concerns about efficiency and accountability. Homeowners are an important group of voters, and lower effective tax rates for them alter their tax–price for additional services, making them more likely to support increased taxes because the taxes will fall (or at least appear to fall) more heavily on others.

Doing nothing fails to address cases of genuine hardship caused by property taxes or to placate homeowners upset by rising property values and taxes, and all states and the District of Columbia have adopted one or more property tax relief

3 The effect is similar to that of differences in tax base composition. When a large percentage of the property tax is from non–residential property, higher property taxes are adopted, probably due to the fact—or at least the perception—of a comparatively low tax–price for the homeowner/voter (Bowman, 1974).
programs. Some relief types are considered next.

**Provide Tax Relief for All Homeowners**

Rapidly rising home values might give rise to general homeowner property tax relief. This might take the form of a homestead exemption for all homeowners, or an equivalent credit. For example, an exemption might reduce assessed value for homeowners by 20 percent before applying the tax rate, so that a $200,000 home would be taxed on only $160,000 of value; if the nominal tax rate is one percent, the tax would fall from $2,000 to $1,600. Alternatively, the one percent rate could be applied to the full $200,000 value with a 20 percent credit allowed, which also would reduce the gross tax from $2,000 to $1,600. Because of their equivalence, exemptions are discussed below and equivalent credits are ignored.

**Uniform Percentage of Value Excluded**

Homeowner tax relief might be the tax on a given percentage of assessed value, such as 20 percent. When the tax relief is a uniform percentage of gross tax for each homeowner, it provides more relief, in absolute amounts, to those with the most valuable houses, but it does not change effective property tax rates (property tax as a percentage of market value) among homeowners. Of course, because the relief is restricted to homeowners, their effective tax rates drop relative to those for other classes of real property.

**Uniform Amount of Value Excluded**

Alternatively, general homestead property tax relief could be the tax on a specified amount of assessed value, such as $50,000 dollars. Because any fixed amount is a larger percentage of total value for less–valuable homes than for more–valuable homes, this approach changes effective property tax rates within the homeowner class, as well as between the homeowner class and other classes of real property. The relative costs of the two approaches depend on many things, including the exemption percentage (first approach) and the exempt amount (second approach), but a greater portion of total relief will go to those with less–valuable homes if relief is the tax on a specified amount of value rather than on a uniform percentage of value. The approaches also differ in how tax relief is affected by rising home values. If relief is the tax on a set amount of value, such as $50,000, no further relief results from increases in home value. Relief equal to a percentage of the gross tax, however, will rise with home value, offsetting a portion of the tax increase. Each approach grants relief to all homeowners, regardless of home value and whether or not it has increased.

**Target Tax Relief to Selected Homeowners**

Because home values rise at different rates across local taxing jurisdictions, and across different neighborhoods within a given jurisdiction, a policy devised as a response to rapidly rising home values might well target relief to some sub–group of homeowners. The possibilities are virtually endless, and I ignore targeting based on such things as age or veteran status to focus on possible problems posed by rising home values that may be experienced by homeowners of all ages, occupations, and other characteristics. The logic of trying to deal with rising tax burdens due to rising home values might lead to

---

4 Several states provide circuit breaker relief to renters, as well as to homeowners, by defining some percentage of rent as property tax paid. The focus of this paper is homeowners, and renter relief provisions are omitted.

5 A classification scheme could be devised to have the same effect as a homestead exemption or credit. Any tax relief approach creates differences in effective rates across property owners, whatever label is attached to it.
either of two bases for targeting property tax relief:

- The more widespread source of concern or irritation is the fact of rising values, which often translate into rising property tax bills. Even property owners who can take the increased taxes in stride tend to dislike higher taxes, so their irritation is of political concern. Relief for those with the greatest rate of value increase is a possible response.

- A smaller number of homeowners experience genuine financial hardship due to rising property values and taxes, as their property tax payments come to account for a large percentage of their incomes and create a cash-flow crunch. Targeting tax relief to those with homestead property taxes above some portion of income is a possible response.

**Target Those Experiencing Rapid Value Increases**

If the perceived problem is rising home values and attendant rising property taxes, regardless of how burdensome the taxes might be, it is possible to grant relief to those whose values are rising most rapidly. Many states have taken this route by capping assessed value increases, limiting the increase in any one year to ten percent, five percent, two percent, or some other specified level. This directly addresses the matter of rising property values, but at a potentially high equity cost: effective tax rates within the homeowner class in a given jurisdiction may come to be quite different; moreover, the lowest effective rates are enjoyed by those reaping the largest gains through rising home values.

In most respects, rising home values are seen as desirable. The increased value can be borrowed against or captured upon sale to use for whatever the owner decides—travel, buying into a retirement community that offers services that may be needed in retirement, leaving a larger inheritance to one’s heirs, or something else. Those experiencing rising property wealth often are regarded as fortunate for their gains are created by market forces—by society—not by their own actions. (Indeed, assessment caps typically exclude value increases due to property improvements.) This socially created benefit is distributed unevenly, even across neighborhoods within a single taxing jurisdiction. Assessment caps compound the disparate experiences, granting additional good fortune to those who enjoy rising home equity by granting them lower effective property tax rates. This is a perverse, inequitable subsidy. Those reaping the smallest socially created windfalls—perhaps even value losses—also must pay higher effective tax rates as a consequence of the relief granted those enjoying larger home equity gains. Because assessed value is reset at time of sale, caps also favor immobility and long-term residents over new ones, with implications for both equity and efficiency.

Suppose, for example, that two homes in a given jurisdiction are each worth $100,000 in a base year, that market value assessment is required, and that the nominal tax rate is one percent. Each homeowner has a $1,000 property tax bill and a one percent effective property tax rate. In the year after the base year, a five percent cap on assessed value increases is put in place; no matter what the increase in market value, the assessed value cannot increase. This directly addresses the matter of rising property values, but at a potentially high equity cost: effective tax rates within the homeowner class in a given jurisdiction may come to be quite different; moreover, the lowest effective rates are enjoyed by those reaping the largest gains through rising home values.

---

6 A study of the Minnesota homestead assessment cap found that 32 percent of homeowners had lower taxes with the cap than they would have had without it, while 68 percent had higher taxes with the cap; the latter included over 250,000 homeowners getting some apparent benefit from the cap who, in reality, were worse off because higher tax rates more than offset their comparatively small assessed value reductions (Haveman, 2005). A similar result is reported for Cook County, Illinois (Dye, McMillen, and Merriman, 2006).
any year. Homes growing in value at five percent or less continue to be assessed at market value, while homes gaining value at a faster rate enjoy fractional assessment. If the value of home A rises at five percent per year, while the value of home B rises at ten percent per year, the owner of B experiences not only more rapid increase in home equity, but also a falling effective tax rate; by contrast, the owner of A continues to pay a one percent effective property tax rate. After five years, the effective tax rate for A is one percent, while that for B is just 0.79 percent, and after ten years, their respective effective tax rates are one percent and 0.58 percent, respectively. This is illustrated by Figure 1, which adds a third home rising in value at 20 percent per year and carries the changes out to 20 years. Significant effective-rate differences emerge in the first year with the five percent cap on assessment increases and grow over time, if value-appreciation differences persist, eventually becoming quite bizarre.

**Figure 1.** Five Percent Assessment Cap Taxes Homes with Highest Market Value Increases at Lowest Effective Rates

![Figure 1](image)

Source: Calculations by author.

Alternatively, the problem of rising home values and property taxes may be seen as property taxes becoming truly burdensome for some, in relation to their income. Relief targeted to such instances would address this problem. It would not grant relief to all whose property taxes have increased due to rising market and assessed values, and it could grant relief to some whose market and assessed values have not risen or have risen at a low rate. A threshold-type circuit breaker is best suited to dealing with this perception of the problem (ACIR, 1975; Bowman, 1980). Circuit breaker property tax relief uses income as the measure of ability to pay property taxes and grants relief that declines as income rises. Over half the states have adopted circuit breaker programs since Wisconsin pioneered the approach over 40 years ago. Their programs differ substantially in the details, but two basic types of circuit breaker have been identified (ACIR, 1975).

- **Threshold**—The threshold approach defines an “acceptable” property tax level as a given percentage of income—the threshold percentage—and grants relief when the property tax exceeds that percent-
age. For example, if the threshold is four percent, relief is granted for property taxes in excess of $200 if income is $5,000, in excess of $400 if income is $10,000, in excess of $1,000 if income is $25,000, and so on. Tax relief may be equal to 100 percent of the tax in excess of the amount determined by the threshold percentage or it may be equal to some fraction of the excess, such as 75 percent (to avoid the adverse incentive of having zero increases in tax liability at the margin when higher tax rates are voted). Some states use multiple threshold percentages that increase with income, which targets relatively more relief to those with the lowest incomes.

- Sliding scale—The sliding scale circuit breaker variant defines several income brackets, or ranges, and specifies a property tax relief percentage for each; the percentage falls as income rises, and at some level of income the relief percentage is zero. For example, the portion of property tax to be relieved might be 95 percent if income is $5,000 or less; 90 percent if income is $5,001–$10,000; 75 percent if income is $10,001–$20,000; 50 percent if income is $20,001–$30,000; and zero if income is above $30,000. States using this approach differ in the maximum relief percentage, how rapidly relief declines, and the income level at which the relief percentage drops to zero. There are notch problems when few income brackets are defined, as a $1 difference in income can result in a much larger increase in the amount of property tax the homeowner is required to bear.

The sliding scale approach will leave the peaks and valleys of property tax burdens in relation to income in place, but at lower levels, while the threshold approach (if no limits are imposed) will lop off all property tax burdens in excess of the threshold percentage. Which approach makes more sense depends upon what causes property tax levels to vary—e.g., differences in housing consumption, public service levels, local government reliance on property taxes, and local government fiscal capacity (Bowman, 1980). If a circuit breaker applies statewide in a state with high property tax reliance and large differences in tax base per capita, the threshold approach is more appropriate. The sliding scale approach makes sense when property tax differences are associated mostly with differences in consumption of housing and/or public services.

Circuit breaker states often impose restrictions, including maximum benefit and income levels. The sliding scale variant inherently has an income ceiling, but the threshold variant need not; housing expenditure typically does not increase in proportion to income as income increases, so relief eventually falls to zero without stating an explicit income ceiling. Net worth limits also may be imposed. Benefit limits often are imposed, in part to avoid encouraging over-consumption of housing. Relieving less than 100 percent of the tax above the threshold percentage of a threshold circuit breaker is another sort of limit. While there are reasons for imposing various limits, they compromise the often-stated intent that rising property taxes should not force people out of their homes. Such tradeoffs need to be recognized and considered. A circuit breaker of any form provides increasing tax relief as property tax bills increase, all else equal, for homeowners who have not reached the program’s ceilings.

Circuit breakers create differences in effective property tax rates both between homeowners and other classes of property and within the homeowner class, much as a homestead exemption equal to a flat amount of value does. However, a well-targeted circuit breaker can provide more
meaningful relief to those most in need of it at a lower total cost, because not all homeowners will qualify for circuit breaker relief. For this same reason, the damage done to equity (defined as uniformity of effective tax rates) is less under the circuit breaker approach.

**Tax Deferral versus Tax Reduction**

Most property tax relief programs reduce property tax liability, but many jurisdictions have adopted property tax deferral programs. The deferred amount can be determined in various ways—like a circuit breaker (defer the “excess” portion of the tax), like an assessment cap (defer the tax in excess of some percentage increase), or in some other way. Typically, interest accumulates on the deferred portion of the property tax. If a market rate of interest is used, deferral is a loan, not a subsidy. Outright tax reduction, by contrast, may be termed a gift. Not surprisingly, outright reduction is more popular among homeowners than deferral—they prefer a gift to a loan.

Reasons given for not liking deferral include not wanting to go back into debt for a home that has been paid for over a working lifetime and wanting to create a larger inheritance for children or grandchildren. Reluctance of intended beneficiaries to avail themselves of deferral programs often is given as a reason not to extend relief in this way. Instead of interpreting low use of deferrals as proof that gifts, not loans, are necessary, it might be taken as an indication that homeowners’ tax problems are not as bad as they would have you believe. This is not to deny that some are truly heavily burdened by high and rising property taxes, but surely not all whose taxes are rising fall into this group. If homeowner property tax problems are not severe enough for owners to take advantage of a loan, are they severe enough to warrant granting subsidies at the expense of others who may not be doing as well as the tax relief recipients?

**Provide Procedural Safeguards to Promote Accountability**

Relief from property tax increases following reassessment might come from appropriate procedural safeguards. If property values are rising at ten percent, 20 percent, or more per year, it is likely that a significant portion of the increase could be offset by reductions in the nominal tax rate. Elected officials often opt for significant property tax levy increases by holding nominal rates constant or by reducing them by a much smaller percentage than the increase in assessed values—yet claim credit for “no tax increase” or a tax reduction. This focuses attention on the assessor, who tends to be blamed for rising taxes. To overcome this, several states have adopted what is variously known as “full disclosure” or “truth in taxation” legislation, to make clear that the elected governing body is responsible for (aggregate) tax increases.

Truth–in–taxation laws require that an increased property tax levy on carry–over properties (those with no new construction or improvements) following reassessment be advertised as a tax increase, with public hearings on the increase, even if the nominal tax rate would be reduced. A small levy increase may be allowed, so that tax–increase advertisements and hearings are needed only for levies that exceed the prior levy on unaltered properties by more than one percent, five percent, or some other level. The governing body can increase the levy, constrained only by any political pressures from constituents. Such a policy seems to have controlled property tax increases in Utah (Cornia and Walters, 2006) and may have helped make
homestead property tax relief—proposed by both major party candidates in the 2005 Virginia gubernatorial election (Bowman, 2005)—a non-issue, despite rapid home value increases in the state.

RESPONSES IN THE DISTRICT OF COLUMBIA, MARYLAND, AND VIRGINIA

To address property tax relief measures in the Washington metro area, Maryland and Virginia state policies, along with some local relief options that have brought different responses in different local jurisdictions, must be described.

District of Columbia

The District of Columbia has many property tax relief programs (District of Columbia Office of Tax and Revenue, 2006). The main programs for the focus of this paper are the following:

- Assessment cap credit,
- Homestead exemption,
- Classification,
- Circuit breaker,
- Senior citizen reduction,
- Lower-income home-buyers’ tax abatement, and
- Deferral.

Assessment Cap Credit

Reassessment is done annually and taxes are calculated using the full assessed value, which is to equal market value. However, a tax increase of more than ten percent for an owner-occupied principal residence due to reassessment (not due to new construction or improvements) results in an automatic credit on the tax bill for the increase in excess of ten percent. This works like a cap on assessed value, but the full assessed value is carried on the tax roll; this may help taxpayers adjust to future increases when the most recent value increase is less than ten percent—for example, two percent—but the assessed value and tax go up by more than two percent. However, the practical difference with annual reassessment seems quite small.

The assessment cap credit was put in place in 2002, when triennial reassessment with three-year phase-in of value increases was abandoned. The cap was 25 percent in 2002, 12 percent in 2003, and ten percent starting in 2004 (Lee, 2006). For lower-income homeowners (adjusted gross income (AGI) between $31,255 and $62,510, depending on household size) who have lived in their homes at least seven years, the assessment cap credit limits reassessment-triggered tax increases to five percent in any year, instead of the generally applicable ten percent limit.

As noted above, such a policy can lead to significant differences in effective property tax rates among homeowners, due to different rates of change in value and length of residence. Restricting the cap to principal residences also creates a differential between year-round and part-year residents, or possibly between domiciled residents and those claiming domicile elsewhere.

Homestead Exemption

The District of Columbia provides a $60,000 “homestead deduction” that exempts $60,000 of value for owner-occupied principal residences. This reduces the taxable assessed value, but it does not rise automatically to offset future assessment increases. For this reason, the District

---

7 The District of Columbia classifies through differential nominal tax rates, which have held steady in recent years. Triennial reassessment and phase-in reportedly resulted in large amounts of foregone property tax revenue (Lee, 2006).
doubled the exempt amount from $30,000 in two stages, in 2005 and 2006.

**Classification**

While the homestead exemption serves to reduce the effective tax rates for homeowners (on their principal residences) relative to other property owners, the District of Columbia also employs a classification scheme that applies lower nominal tax rates to residential properties. Currently, the rates are 0.92 percent for residential properties, 1.85 percent for commercial properties, and five percent for vacant properties. Several years ago, there were two residential classes (class 1, owner-occupied residential; class 2, other residential) and two commercial classes (class 3, hotels and motels; class 4, other commercial) in a five-class system; the lowest nominal rate applied to owner-occupied residences, which also received a $30,000 homestead exemption (Bowman, 1998, 127–9 and 152–3). Thus, the classification system has been simplified with the nominal rates for classes 2 and 4 being lowered significantly in the process. The direction of this change is appropriate, but it underscores the tradeoffs in property tax policy—taken alone, the change diminished the classification advantage for owner-occupied residential properties. This put more of the total property tax on owner-occupied residences, which is at odds with current concerns over mounting tax burdens for homeowners. The recent doubling of the homestead exemption to $60,000 provides an offset to this earlier change.

**Circuit Breaker**

The District of Columbia has two threshold-type circuit breaker programs. The program for those under age 62 has six thresholds, ranging from 1.5 percent of the first $2,999 of income to four percent of income between $15,000 and $20,000. At the lowest income level, 95 percent of “excess” property tax is relieved; otherwise, only 75 percent of excess tax is relieved. By contrast, for those at least 62 years old, there are only four thresholds, ranging from one percent on the first $4,999 of income to 2.5 percent on income between $15,000 and $20,000, and 100 percent of excess tax is relieved. For both age groups, however, the maximum property tax relief is $750, and the maximum qualifying income is $20,000. Moreover, as with many circuit breaker programs, income is defined quite broadly—and quite appropriately—to include essentially all money income.

The circuit breaker for the elderly group clearly is the more generous of the two, until the limits are hit. For example, the maximum benefit of $750 is reached for non-elderly homeowners when income is $1,500 or less and the property tax is at least $800, which is the tax on a home worth about $147,000; for the elderly, the limit is reached if income is $2,000 or less and the property tax is at least $760, which is the tax on a home worth about $143,000 (or about $225,000 if the owner qualifies for the additional elderly tax reduction discussed below). At the other end of the eligible income range, the $750 benefit maximum is reached by the non-elderly when income is $19,001–$20,000 and property tax is at least $1,780, which is the tax on a home worth about $253,000; for the elderly, the benefit ceiling is reached when income is $19,001–$20,000 and property tax is at least $1,240, which is the tax on a home worth about $195,000 (or about $330,000 for an owner who qualifies for the additional elderly tax reduction).

Although property tax relief favoring the elderly—often even excluding non-elderly homeowners from property tax relief programs—is common across the country, the most obvious rationale for this is the voting power represented by the elderly. Financial hardship is not restricted to the elderly;
indeed, the incidence of poverty has been higher among the non–elderly than among the elderly for approximately two decades, and the elderly are more likely to have no mortgage.

The District’s circuit breaker benefit and income limits are too low for this to be the major program for dealing with any hardships caused by escalating home values, particularly in an area with such high housing costs, but a more generous circuit breaker could serve this function.

Senior Citizen and Disabled Tax Reduction

Homeowners who are at least 65 years old or disabled are eligible for a 50 percent property tax reduction, provided total household AGI is under $100,000. This reduction is in addition to the $60,000 homestead exemption.

Lower–Income Homeowners’ Tax Abatement

Lower–income households (AGI between $32,155 and $62,510, depending on household size) buying a home valued at less than $264,000 may qualify for a five–year abatement of property taxes. This makes buying a home more feasible, but after five years, any tax break must come from the other programs, including—after seven years—the lower–income homeowners’ five percent assessment cap credit, already noted.

Deferral

If household AGI is $50,000 or less, an elderly taxpayer can defer the total property tax bill, while younger taxpayers can defer the increase in excess of ten percent. The interest rate for deferred taxes is eight percent, and the total of deferred taxes plus interest cannot exceed 25 percent of the assessed value of the home. For the non–elderly, the deferral option now seems irrelevant, for the assessment cap credit adopted in 2002 relieves any property tax increase in excess of ten percent, if caused by reassessment.

Maryland

Maryland also provides more than one form of property tax relief applicable to homeowners (Maryland Department of Assessments and Taxation, 2006). These are:

- Phase–in of increases in assessed value,
- Assessment cap credit, statewide but with enhancement at local option,
- Circuit breaker, statewide but with enhancement at local option, and
- Local–option deferral.

Phase–In of Increased Assessed Values

Maryland has a three–year, staggered reassessment cycle; each year, some local jurisdictions are reassessed, and each jurisdiction is reassessed every three years. The assessment standard is 100 percent of market value. However, one–third of any value increase determined in a reassessment is added to assessed value in each of the three years of the cycle, so the assessed value will equal the market value determined in the most recent reassessment only in the last year of the triennial cycle. For example, if a home is revalued from $150,000 to $205,500, assessed value is increased by one–third of the $55,500 increase in each of the next three years, giving assessed values of $168,500, $187,000, and finally, $205,500.

This phase–in reduces the assessed value increase in any one year for all property owners, not just homeowners and not just those whose properties are rising in value at very high rates. However, it also keeps effective property tax rates below the nominal tax rate because the assessed value does not rise to the market value on the tax roll until that value is three years old.

Assessment Cap Credit (“Homestead Credit”)

As in the District of Columbia, taxes on unaltered principal residences cannot rise more than ten percent in any year, and this
cap is provided through a tax credit for increases in excess of ten percent rather than through actual reductions of assessed value. The ten percent limit applies statewide; since 1990, local governments in Maryland have been free to set the limit lower than ten percent. Of the 23 counties and the independent city of Baltimore, all but nine have gone to a lower limit. At the extreme, one county allows no increase in homeowner taxes due to reassessment and another sets the limit at two percent; the most common limits are ten percent (nine counties)—the maximum allowed by the state—and five percent (seven counties). In the immediate Washington, D.C., area, Prince George’s County caps increases at three percent while Montgomery County sets a ten percent cap; within Montgomery County, however, Kensington imposes a five percent cap.

Differences in effective property tax rates among homeowners can become more extreme as the percentage cap drops. As in the District, Maryland creates a differential between year-round resident homeowners and part-year residents, for the cap applies only to principal residences. In Maryland, assessment caps—especially low caps—exacerbate the suppression of assessed value below market value caused by the phase-in of value changes over three years.

Circuit Breaker

Maryland has a statewide, state-funded circuit breaker relief program for owners (and renters) of all ages. It, too, is of the threshold variety and employs multiple thresholds but, unlike the District of Columbia, Maryland has a single program for all ages. After liberalization in 2006, the “acceptable” amount of tax is zero percent of the first $8,000 of income, four percent of the next $4,000 of income, 6.5 percent of the next $4,000 of income, and nine percent of income in excess of $16,000; as is typical of circuit breaker programs, income is quite broadly defined. There is no ceiling on the amount of income a taxpayer may have to be eligible, and no limit on the amount of relief as such, but there are other limits. Specifically, net worth—excluding the value of the residence and, starting in 2006, most qualified retirement accounts—must be under $200,000; moreover, while an owner-occupant with a home of any value may be eligible for circuit breaker relief, the tax on the amount of assessed value in excess of $300,000 is ignored (doubled in 2006). To give an indication of the degree to which property taxes are relieved, and how rising income affects the relief amount, it is noted that any tax above $80 is relieved if income is $10,000, while the threshold, or acceptable, amount of tax at $30,000 and $100,000 are, respectively, $1,680 and $9,980. Because only the tax on up to $300,000 of income is considered, a property tax bill of $9,980 implies a tax rate of 3.33 percent, which is higher than the rate of any county, city, or town for tax year 2005–2006. Although Maryland has opted to provide relief through other programs, as well, a circuit breaker of this sort could provide the primary or sole program for dealing with rising taxes due to rising home values.

Local-Option Deferral

Maryland law allows localities to adopt a property tax deferral program for homeowners at least 65 years of age (Montgomery County is able to offer deferral regardless of age), who may defer the increase in the tax after some base period. Local governments have authority to set income limits and to set interest rates applicable to deferred tax amounts.

Virginia

Unlike the District of Columbia and Maryland, Virginia has no statewide form of property tax relief, other than the truth-in-taxation program (Knapp, 2005). However, state law authorizes
certain local–option real property tax relief programs applicable to homeowners (Knapp, Shobe, and Kulp, 2005, 21–38). The Virginia programs are:

- Truth–in–taxation, excluding a one percent allowable levy increase,
- Homestead exemption or deferral for the elderly or disabled, at local option, and
- Homestead tax relief for other homeowners, at local option for a few localities.

Virginia has 134 primary assessing units (95 counties and 39 independent cities) with varying reassessment cycles. Reassessment is required every two years, four years, or six years, depending upon the type of unit (city or county) and its population size. More frequent reassessments may be conducted if a local unit chooses, and 17 cities and 11 counties have gone to annual reassessment (Virginia Department of Taxation, 2006, Table 1). More frequent reassessment may reduce taxpayers’ reassessment shock because they capture fewer years’ value increases at one time, but if annual increases are large, reassessment still will be unpopular.

Truth–in–Taxation

Virginia state law restricts local government ability to translate increased assessed values into increased tax levies by imposing a procedural requirement on local governments following reassessment, to increase public awareness of any tax increases and to make clear that responsibility rests with the local governing bodies, such as city councils and county boards of supervisors—not with the property tax assessor. Specifically, following reassessment, if a taxing unit wishes to levy property taxes more than one percent higher than in the preceding year on the same properties (i.e., excluding new construction), the governing body must advertise and hold hearings on a tax increase, even if the nominal tax rate would be lowered. For example, if reassessment increases assessed values by 30 percent and the tax rate is cut by 15 percent—from one percent to 0.85 percent—the truth–in–taxation requirements would apply.

Local–Option Relief for Elderly and Disabled Homeowners

Virginia law also authorizes local units of government to adopt property tax relief for elderly (65 and over) and disabled homeowners, in the form of either a homestead exemption or a tax deferral. Income and net worth limits are prescribed by the state. In general, the gross combined income of the owner and all relatives living in the dwelling unit is limited to $50,000, but up to $10,000 income of each relative (except the spouse) may be omitted if the locality chooses. The general net worth limit is $200,000, excluding the value of the dwelling unit and up to ten acres of land. In 2004, higher limits were authorized for counties with over 800,000 population (Fairfax County) and adjacent counties and cities to $72,000 income and $340,000 net worth.

Property tax relief measures have been adopted by 121 of the 134 counties and independent cities, including all those in the Washington, D.C. vicinity. (Several towns, which are constituent units within counties, also have adopted property tax relief.) Of these, two counties and one city provide relief for the elderly only; all others provide relief for both elderly and disabled homeowners. Most localities provide exemption rather than deferral, but several combine exemption and deferral; exemption commonly is provided in the manner of a sliding scale circuit breaker. Alexandria provides an example of both the circuit breaker approach and the inclusion of deferral. The exempt portion is 100 percent if income is $40,000 or less, 50 percent if income is $40,001–$50,000, and 25 percent if income is $50,001–$62,000.
however, those able to exempt less than 100 percent can defer the remainder at five percent interest. Besides the $62,000 income limit, the net worth limit in Alexandria is $240,000. Among the four Virginia counties and five independent cities in the Washington area, the 2005 income limits range from $30,000 (Falls Church) to $72,000 (Arlington County and Loudoun County), net worth limits range from $100,000 (Falls Church) to $340,000 (Fairfax, Loudoun, and Prince William counties), and the circuit breaker approach is used by seven localities (all but Falls Church and Loudoun County). Most of these jurisdictions liberalized their relief provisions in some respect between 2004 and 2005, but not all had taken advantage of what the state now allows in this part of Virginia. Statewide, city income limits range from $15,000 to $62,000 (median = $62,000) and the net worth limits range from $25,000 to $240,000 (median = $77,500). County income limits range from $7,500 to $72,000 (median = $24,000) and the net worth limits range from $30,000 to $340,000 (median = $75,000).

Local-Option Relief for Other Homeowners

More recently, a few localities have gained authority to offer property tax relief to some homeowners who are not elderly or disabled. Alexandria adopted such a program in 2004 and liberalized it in 2006; called an affordable housing preservation grant, the program provides a property tax credit that varies with household income and size (Alexandria Finance Department, 2006). Under the new provisions, the credit is $1,200 (if income is $40,000 or less), $875 (if income is $40,001–$55,000), $375 (if income is $55,001–$72,000), or $200 (if there are at least two people in the household and income is $72,001–$87,000 or at least three in the household and income is $87,001–$100,000). Net worth cannot exceed $50,000, excluding the dwelling, up to two acres of land, household furnishings, personal motor vehicles, and qualified retirement accounts. Before 2006, the income ceiling was $62,000 and the maximum credit was $675. In 2006, the General Assembly approved a charter change for Charlottesville to allow a similar program, and the city council is considering a $250 “grant” for homeowners with income below $50,000 and home value below $238,200 (Yellig, 2006).

CONCLUDING COMMENTS

The District of Columbia and Maryland provide property tax relief that directly addresses concerns about rising home values, most notably through their assessment cap credits; in addition, Maryland phases in assessed value increases over a three-year period. Both the District and Maryland provide other forms of property tax relief that also soften the impact of rising assessed values for homeowners. Their circuit breakers are best suited to this task, in that property taxes that rise more rapidly than income tend to increase circuit breaker relief. The low benefit and income limits of the District’s circuit breaker, however, seriously weaken its ability to play this role. The District’s fixed-dollar homestead exemption would have provided no offset against rising assessed values if the amount had not been increased by statutory change, doubling it from $30,000 in 2004 to $60,000 in 2006.

By contrast, Virginia’s only statewide program bearing on the matter of rising assessed values is the truth-in-taxation law, which provides procedural safeguards that attempt to make clear that responsibility for tax levies that rise significantly following reassessment rests with the local governing bodies rather than with the assessors. Because
this program leaves the local governing bodies free to adopt higher tax levies after advertising the increase and holding public hearings, it often is viewed as a weak tool for dealing with homeowners’ concerns. However, dissatisfaction with the property tax in Virginia apparently is relatively low because it failed to become an issue in the 2005 gubernatorial campaign, even though one candidate proposed a 20 percent homestead exemption and another proposed a five percent assessment cap, both for homeowners of all ages. Moreover, Cornia and Walters (2006) report that a truth–in–taxation program in Utah (where it is known as “full disclosure”) seems to have been effective, in that the property tax dropped relative to personal income after imposition of the truth–in–taxation program, even though caps on assessment increases were removed.

The Utah and Virginia circumstances provide some hope that more drastic property tax changes might not be needed. Most damaging to the uniformity of effective tax rates that is so important for equity and for the logic of the tax as a tax on property value (i.e., market value) are caps on assessment increases. These caps, whether they actually limit assessed values on the tax rolls or provide relief through equivalent credits against tax liabilities calculated using unconstrained values, can result in very substantial differences in effective property tax rates within the homeowner class. They provide the lowest effective property tax rates for homeowners who have been fortunate enough to enjoy the largest socially created windfall gains in their home values—and, thus, their net worth. Imposing higher effective tax rates on those whose net worth (home equity) is growing slowest to further subsidize those gaining most through market (social) forces is perverse and is a serious departure from sound property tax policy.

This is not to deny that rapidly rising home values and consequent increases in property taxes can cause hardship. However, the most logical and fairest way to deal with rising homeowner taxes due to rising home values is to target relief to those who experience true hardship as a result. Such hardship may be measured by the level of property tax relative to a broad measure of income. Although most homeowners may prefer an outright property tax reduction to a loan (deferral of tax, at interest), this is hardly a sound reason for giving gifts rather than loans to those who are benefiting from socially created gains in net worth. In contemplating such outright tax reductions, careful consideration should be given to their equity effects, both within the property tax and more broadly (the comparative incidence of the increases in other revenues and/or service cuts needed to finance generous homeowner tax relief). If, in the end, the political judgment is that tax reduction, rather than deferral, is to be provided, a well–designed circuit breaker seems the best tool for the job.

Residential property tax relief measures have been adopted or liberalized in recent years in the District of Columbia, Maryland, and Virginia; in Virginia, there has been some loosening of the state’s restrictions on local-option relief and subsequent liberalization by several local governments. However, deferral remains rather unimportant in the two states and the District, Virginia has no state–level circuit breaker, and the District’s low circuit breaker limits have not been eased. Maryland this year adopted circuit breaker changes that significantly liberalize that program, but other recent major changes have been the District’s new assessment cap credit and lower caps set by several Maryland local governments. Those of us who advocate a more uniform property tax face a challenging environment.
REFERENCES

Advisory Commission on Intergovernmental Relations (ACIR).


Alexandria Finance Department.


Bowman, John H.


Bowman, John H.


Bowman, John H.


Bowman, John H.


Cornia, Gary C., and Lawrence C. Walters.


District of Columbia Office of Tax and Revenue, Real Property Service Center.

Website with links to property tax relief programs. (June 11, 2006). http://otr.cfo.dc.gov/otr/site/default.asp.

Dye, Richard F., Daniel P. McMillen, and David F. Merriman.


Haveman, Mark.


Knapp, John L.


Lee, Fitzroy.

Telephone conversation between the author and Dr. Lee, in the District of Columbia Office of Tax and Revenue, May 12, 2006.

Maryland Department of Assessments and Taxation.


Maryland Department of Assessments and Taxation.

Website with links to property tax rates, tax relief, and tax administration information. (May 10, 2006). http://www.dat.state.md.us/.

U.S. Bureau of the Census.

U.S. Office of Federal Housing Enterprise Oversight (OFHEO).
Virginia Department of Taxation.
Yellig, John.