How do state and local property taxes work?

Jurisdictions in all 50 states and the District of Columbia impose property taxes. Most property tax revenue comes from levies on land and improvements, but states often tax personal property (such as machinery, equipment, and motor vehicles) as well. The tax equals a percentage of the taxable value of the property and may be levied in some form at every level of government: state, county, municipal, township, school district, and special district.

HOW MUCH REVENUE DO STATE AND LOCAL GOVERNMENTS RAISE FROM PROPERTY TAXES?

While property taxes are a significant source of local government revenue, they are a very small revenue source for most states (table 1). State governments levy property taxes in 36 states, collecting $13 billion in revenue from such taxes in 2013—about 1 percent of own-source general revenue ("own-source" revenue excludes intergovernmental transfers). Vermont relied on property taxes for 26 percent of state own-source general revenue in 2013, far and away the highest percentage in any state. Property taxes were 5 percent or more of state revenue in only six other states: Arkansas, Michigan, Montana, New Hampshire, Washington, and Wyoming. Fourteen states did not levy a state-level property tax.

Local governments depend much more on property tax revenue. Local governments collected $442 billion from property taxes in 2013—47 percent of own-source general revenue. Property taxes provide three-quarters or more of local own-source revenue in six states; Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, and Rhode Island.

TABLE 1

State and Local Property Tax Revenue

2013

	Revenue (billions)	Percentage of own source general revenue
State and local	$455	22%
State	$13	1%
Local	$442	47%

Source: Urban-Brookings Tax Policy Center, State & Local Government Finance Data Query System

Note: Own source general revenue does not include intergovernmental transfers.

Property taxes are the largest own-source of revenue for counties, cities, townships, school districts, and special districts, which are specific-purpose units, such as water and sewer authorities. School districts rely quite heavily on property taxes, collecting $181 billion in 2012, which was 82 percent of their own-source general revenue. Because school districts receive substantial intergovernmental transfers, own-source revenue makes up less than half (about 45 percent) of their total general revenue.

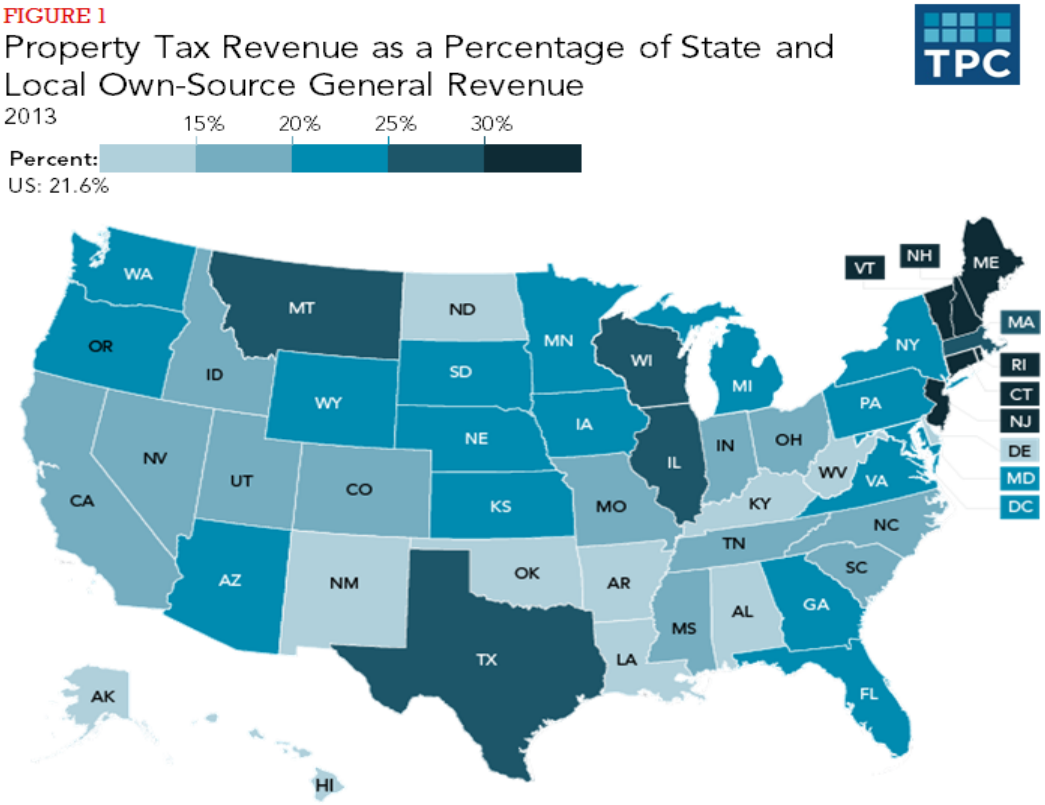
IN WHICH STATES ARE PROPERTY TAXES MOST IMPORTANT?

New Hampshire, which has neither a broad-based income tax nor a general sales tax, was the most reliant on property taxes in 2013, with property tax revenue accounting for 44 percent of combined state and local own-source general revenue. Property taxes also contributed more than 30 percent of state and local revenue in Connecticut, Maine, New Jersey, Rhode Island, and Vermont. All told, 11 states, including seven in the Northeast, collected at least one-quarter of their state and local own-source general revenue from property taxes (figure 1).

FIGURE 1

Property Tax Revenue as a Percentage of State and Local Own-Source General Revenue

2013



Source: Urban-Brookings Tax Policy Center, State & Local Government Finance Data Query System.
Note: Own source general revenue does not include intergovernmental transfers.

North Dakota relied least on property tax revenue in 2013, with less than 10 percent of its combined state and local own-source general revenue generated from property. Eleven states collected less than 15 percent of combined state and local revenue from property taxes.

HOW MUCH DO PROPERTY TAX RATES DIFFER ACROSS THE COUNTRY?

Effective property tax rates differ widely across and within states, making them difficult to compare. In addition to variation in statutory tax rates, local governments use various methods to calculate their real property tax base.

The taxing jurisdiction typically assesses the real property value by estimating what the property would sell for in an arms-length transaction. However, some jurisdictions base value on the last sale price or acquisition value of the property, others consider the income that a property could generate (for example, an empty lot that could be used for a hotel), and some base the assessment solely on the size or physical

attributes (e.g., design, location) of the property. There is also variation in the timing of assessments, with some jurisdictions assessing annually and others less frequently.

Some jurisdictions tax the entire assessed value of the property (before deductions and credits). Others tax only a fraction of the assessed value. For example, counties in South Carolina tax only 4 percent of a property's assessed value. Jurisdictions may impose different statutory tax rates ("classifications") for different types of property, most commonly distinguishing between residential and business property.

HOW DO STATES LIMIT PROPERTY TAXES?

In recent decades, many states have imposed limits on property tax rates, property tax revenue, or increases in assessed property values, reducing reliance on the property tax as a source of revenue. California, for example, limits the tax rate to 1 percent and annual assessment increases to 2 percent until a property is sold. As a result, neighbors with similar houses may have dramatically different tax liabilities depending on when their houses last changed hands.

States and local governments also often use limits, exemptions, deductions, and credits to lower tax liability. Here are some examples:

- Assessment limits prevent a property's assessed value from increasing by more than a fixed percentage between assessments. These limits can reduce a property's assessed value below its market value and prevent rapid property value increases from raising the owner's tax burden. When the property is sold, its assessed value is reset at market value.

- Homestead deductions and exemptions decrease the taxable value of real property by a fixed amount (much the same way a standard deduction decreases taxable income) for residents who occupy the property. Forty-one states and DC have homestead exemptions that reduce the fraction of the assessed property value subject to tax.

- Circuit breaker programs provide relief for elderly and low-income residents with property tax liabilities above a specified percentage of their income. Although relief is based on property tax payments, it is typically provided via an income tax credit. In most states, the state government collects income tax while local jurisdictions collect property tax, making circuit breakers a type of subsidy from state to local governments. Unlike the other approaches described here, circuit breakers benefit renters as well as homeowners in some

jurisdictions. Twenty-eight states and the DC use circuit breaker credits and refunds to limit the share of income claimed by property taxes.

- Property tax deferrals allow elderly and disabled homeowners to defer payment until the sale of the property or the death of the taxpayer. All told, 22 states and the DC allow such deferrals, but they are not widely used.

DATA SOURCES

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