Infrequent Assessments Distort Property Taxes: Theory and Evidence

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Working Paper

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Abstract

Economists have long recognized that lags in property reassessment benefit infrequent movers because the lags reduce their property taxes. But in addition, assessment lags can influence the level of property taxes selected under majority rule. I show that short assessment lags increase property taxes because a majority of voters face a relatively low tax price. However, longer lags reduce the aggregate assessed base so much that property taxes begin to decline. I formally characterize the cutoff between these regimes and show taxes are generally above their socially optimal level. This theory can help explain why many people believe property taxes are excessive and can only be reduced with a formal tax limit; it also suggests that the American system of taxing capital gains at realization, rather than on accrual, might result in super-optimal rates.

I test this theory on a sample of Pennsylvania municipalities in the Philadelphia suburbs. This is an excellent crucible for examining the role of reassessments because they are infrequently performed in Pennsylvania. It is not possible to reject the theory's basic predictions, and numerical estimates suggest that a five-year gap between reassessments increases government revenues six percent above their socially optimal level. However, assessment delays do not impose statistically significant social losses because they benefit infrequent movers.

JEL classification: D7, H7
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