How Limits on Assessment Increases in Tax Class 1 Lead to Tax Burden Disparities

The limits on assessment increases in Tax Class 1 mean assessments can grow at different rates than market values, creating disparities in the tax burden between properties experiencing different rates of appreciation. This is illustrated by considering two hypothetical new $500,000 Tax Class 1 properties that enter the tax rolls in 2015. One of these houses is located in an area where market values are appreciating by 10 percent per year while the other is in an area with 2 percent annual appreciation. In the first year, both properties are assessed using the target assessment ratio of 6 percent of market value, and they have identical property tax bills of $5,747, resulting in identical effective tax rates (taxes per $100 of market value) of $1.15.

The tax burdens begin to diverge in the second year. For the rapidly appreciating property, the assessment increase is capped at 6.0 percent, resulting in an assessment of $31,800 and an assessment ratio of 5.8 percent. The assessment on the slower appreciating property can grow by 6.0 percent to $30,600, meaning the assessment ratio and effective tax rate is higher for the slower appreciating property than for the faster appreciating one. Note that while the effective tax rates are lower for the slower appreciating property, the tax liability grows faster for the more rapidly appreciating property—over 8 percent annually in years 2, 3, and 4 versus a bit over 4 percent for the former.

The differences continue to grow in the third and fourth years. In the latter year, the difference in effective tax rates is 11.9 percent ($1.21 versus $1.09). In the fifth year, the second level of the assessment increase limit kicks in and limits increases to no more than 20.0 percent over five years. For the rapidly appreciating property, the assessment increase from 2018 to 2019 is only 0.8 percent, even as the market value grew by 10.0 percent. For the slower appreciating property, the fifth year increase is 2.0 percent, mirroring the market value appreciation, as the assessment growth over the five years has been well below the 20.0 percent limit. The difference in effective tax rates is 22.0 percent. Assuming these rates of market value appreciation continue in years after 2019, the disparities would continue to grow.[1]

Effective Tax Rates Diverge Over Time Depending on Rate of Market Value Appreciation

	Property With 10 Percent Annual Appreciation				
	2015	**2016**	**2017**	**2018**	**2019**
Market Value	$500,000	$550,000	$605,000	$665,500	$732,050
Target Assessment Ratio	6.0%	6.0%	6.0%	6.0%	6.0%
Target Assessment	$30,000	$33,000	$36,300	$39,930	$43,923
Actual Assessment With Limits	$30,000	$31,800	$33,708	$35,730	$36,000
Actual Assessment Ratio	6.0%	5.8%	5.6%	5.4%	4.9%
Tax Rate	19.157%	19.554%	19.991%	20.385%	20.919%
Tax	$5,747	$6,218	$6,739	$7,284	$7,531
Effective Tax Rate (Tax /$100 of Market Value)	$1.15	$1.13	$1.11	$1.09	$1.03
	Property With 2 Percent Annual Appreciation				
	2015	**2016**	**2017**	**2018**	**2019**
Market Value	$500,000	$510,000	$520,200	$530,604	$541,216
Target Assessment Ratio	6.0%	6.0%	6.0%	6.0%	6.0%
Target Assessment	$30,000	$30,600	$31,212	$31,836	$32,473
Actual Assessment With Limits	$30,000	$30,600	$31,212	$31,836	$32,473
Actual Assessment Ratio	6.0%	6.0%	6.0%	6.0%	6.0%
Tax Rate	19.157%	19.554%	19.991%	20.385%	20.919%
Tax	$5,747	$5,984	$6,240	$6,490	$6,793
Effective Tax Rate (Tax /$100 of Market Value)	$1.15	$1.17	$1.20	$1.22	$1.26

NOTE: Tax rates are adopted Tax Class 1 rates for each year

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Endnote

[1]Even if the rates of appreciation were to converge, the disparities in effective tax rates would persist for years after such a convergence as it takes many years to recover the “lost” assessment growth.

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