Property Tax Relief in Pennsylvania

PENNSYLVANIA
Budget and Policy Center

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One of the primary issues being negotiated in the 2015-16 budget is school property tax relief. There are several proposals being considered. Each one would distribute relief differently. In this brief, we describe the basic mechanisms of property tax relief available in Pennsylvania and explain which form of relief is most likely to benefit which type of property owner (owners of modestly priced homes, high-priced homes and non-residential properties). This basic primer on property tax relief lays a foundation for forthcoming analysis of the specific proposals now being debated as part of the state's budget debate.

Property taxes are unpopular, yet are the primary tax revenue source for our schools, counties, and municipalities. Property taxes are among the easiest taxes to administer and are difficult to avoid – as real property (unlike income, capital, sales, or other transaction-based taxes) is not mobile. Property taxes are also the easiest way for local governments to tax corporations and other business entities with complex ownership arrangements so that these users of public services also contribute to the costs of providing schools, police, and fire protection.

Pennsylvania Requires Uniform Rates

The Pennsylvania Constitution includes a "uniformity clause" that requires that if the state or a local government has a tax on something, it must use the same tax rate for everything subject to that particular tax (in other words, a "uniform" rate).[1] For property taxes, this means that all types of real property that are subject to property taxes must be charged the same tax rate. In other states, it is not uncommon for homes to be charged a different tax rate than factories, offices, or other commercial property. This is not permitted in Pennsylvania.

Preferential Property Tax Treatment for Farms and Forestland

For farms and forests, a special assessment[2] is permitted under which qualifying land is valued at the agricultural use value, rather than market value. This lowers the property taxes owed by farmers - who are often land rich, but may lack income and other forms of wealth -- and can help lower the pressure on farmers to develop their land for other purposes. This preferential treatment often increases taxes paid by non-farm properties in rural districts.

[1] Pennsylvania Constitution, Article VIII, Section 1, http://sites.state.pa.us/PA_Constitution.html.
[2] Pennsylvania Constitution, Article VIII, Section 2(b)(i), http://sites.state.pa.us/PA_Constitution.html.

Special Property Tax Relief Available for Homeowners

The Pennsyvlania Constitution was changed in 1997 to allow property tax relief for homeowners. Rather than allowing different tax rates for homeowners than non-residential property owners, the constitution's "homestead exemption" exempts owners of qualifying owner-occupied housing from paying property taxes on the first part of residential property value, up to one-half of the value of the median home value (or "homestead").[3] In effect, this provision operates similarly to personal exemptions on federal taxes, except that the homestead exemption eliminates taxes on the first part of qualifying residential property value rather than the first part of income.

Property Tax Benefits for Senior Homeowners and Renters

Pennsylvania established the Property Tax/Rent Rebate Program (PTRR) in 1971 to help senior citizens, widows and widowers age 50 and over, and adults with disabilities pay for housing costs. Both homeowners and renters can qualify for PTRR.[4]

Renters with annual household incomes up to $8,000 can receive a rebate up to $650. Those with annual incomes from $8,001 to $15,000 can receive a rebate of $500. Although the rebate amounts have increased, the income eligibility for renters has not been raised since 1985.

Income eligibility for homeowners is higher, up to $35,000 a year. The base maximum rebate available to homeowners is $650 for individuals with annual incomes up to $8,000. Homeowner benefits decrease in steps as income rises. Those earning between $18,001 and $35,000 a year can receive a rebate of $250.

In addition to the base amount, homeowners earning up to $30,000 a year who either live in certain higher cost areas (Philadelphia, Scranton and Pittsburgh), or who pay more than 15% of their income in property taxes, receive an additional 50% rebate payment – increasing the total rebate to a maximum of $975.

The PTRR benefits could be increased, if assistance is to be focused on the elderly.

In 2013, PTRR provided $270 million in rebates to over 565,000 recipients.[5] These rebates were funded out of the Pennsylvania Lottery and taxes collected from casino gaming.

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[3] For a fuller explanation, see Pennsylvania General Assembly, Local Government Commission, *Pennsylvania Legislators' Municipal Deskbook*, Third Edition (2006), pp. 148-149, http://www.lgc.state.pa.us/deskbook06/Issues_Taxation_and_Finance_02_Homestead_Exemption.pdf.

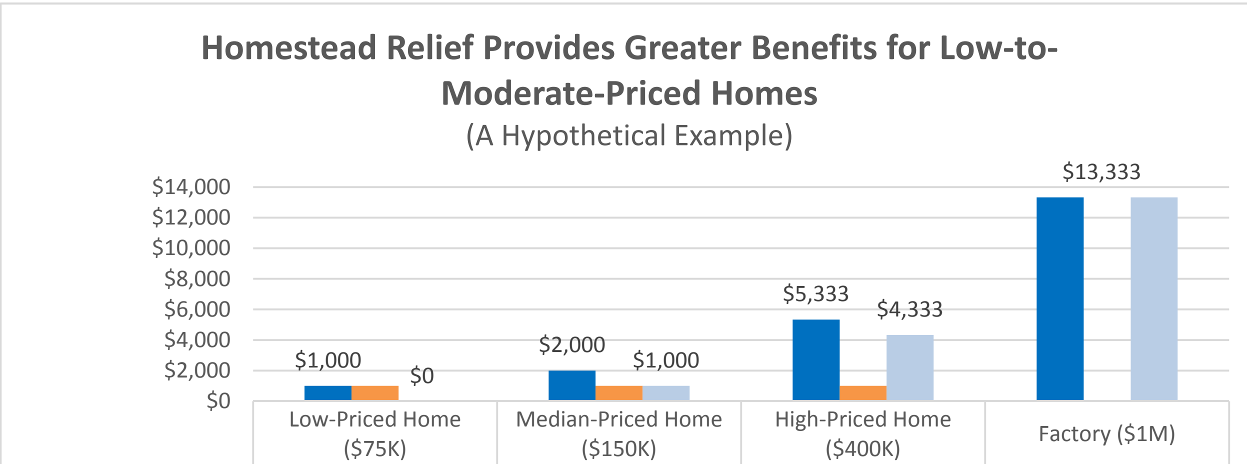
[4] This special tax treatment for seniors and the disabled is permitted by Pennsylvania Constitution, Article VIII, Section 2(b)(ii), http://sites.state.pa.us/PA_Constitution.html.

[5] Pennsylvania Department of Revenue, Bureau of Research*, Report to the Pennsylvania General Assembly on the Property Tax Rent Rebate (PTRR) Program for Property Taxes or Rent Paid in 2013*, September 30, 2014, http://www.revenue.pa.gov/GeneralTaxInformation/News%20and%20Statistics/Documents/PTRR%20Reports/2014_ptrr_report.pdf.

Homestead Relief Typically Better for Middle-Class Homeowners

Figure 1 shows how this type of relief works. In this example, the constitutional limit of homestead relief ($1,000 – half of the median homestead's tax bill) is provided to all homesteads. This $1,000 per homestead relief provides greater relative benefit to owners of low-to-moderate-priced homes, and less relative relief to owners of higher-priced homes. No relief is given at all to owners of non-homestead properties.

Figure 1.



	Low-Priced Home ($75K)	Median-Priced Home ($150K)	High-Priced Home ($400K)	Factory ($1M)
Before	$1,000	$2,000	$5,333	$13,333
Homestead Relief	$1,000	$1,000	$1,000	$0
After	$0	$1,000	$4,333	$13,333

Source. Pennsylvania Budget and Policy Center

Critics of homestead relief worry that reducing the tax rates of homeowners can relieve local pressure to keep overall property tax rates as low as possible. Unlike homeowners, other property owners may not live in the taxing jurisdiction, so they have less of a direct vote on who makes property tax decisions.

This concern overlooks state limits already in place and the political reality. Since 2006, there have been state limits on school district property tax increases (Act 1 index).[6] If a school district wishes to increase property taxes by a rate greater than its index, it must have direct approval of the rate increase by voters. The Act 1 base index for 2015-16 is 1.9%, with a higher index applying in less affluent districts.[7]

The second factor is that school board members are not anxious to raise property tax rates. The limits of homestead relief mean that the typical homeowner still pays property taxes and would have to pay a large share of any increase.

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[6] Pennsylvania Department of Education, "Act 1 Index," http://www.portal.state.pa.us/portal/server.pt/community/property_tax_relief/7452/act_1_index/510332.

[7] Pennsylvania Department of Education, "The Index, Special Session Act 1 of 2006," http://www.portal.state.pa.us/portal/http;//www.portal.state.pa.us;80/portal/server.pt/gateway/PTARGS_0_123706_1437251_0_0_18/SSAct1%20BaseIndexHistory%200607-1516.pdf.

Millage Rate Cuts Tilt Benefits to Wealthier Homeowners and Business Property Owners

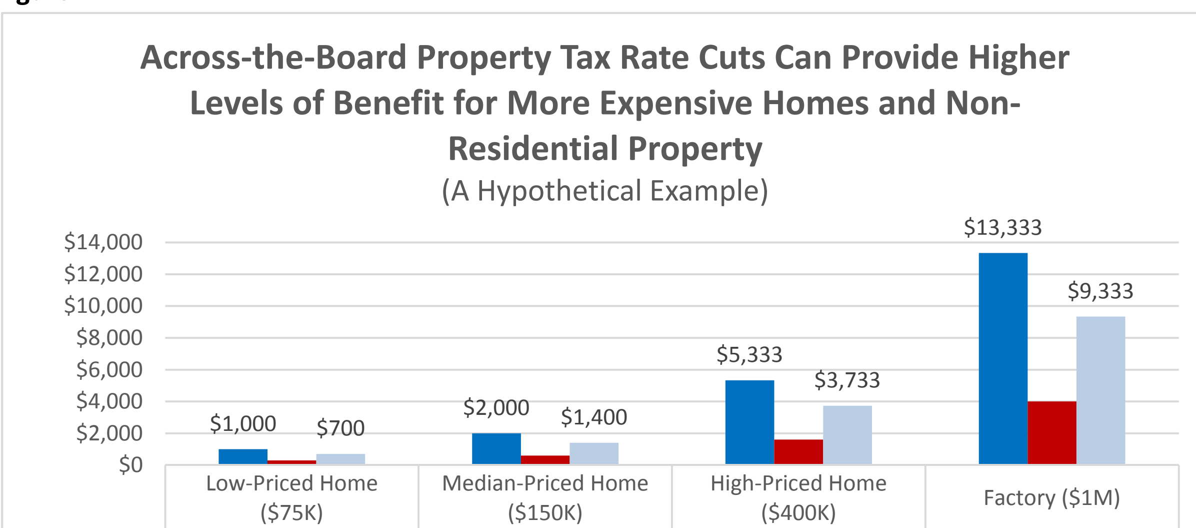
Rather than focusing benefits on homeowners (homesteads), property tax relief could be used to lower tax (or "millage") rates across-the-board. This means that all types of property -- including malls, factories, and golf courses -- receive the same percent rate reduction as a homeowner in the district. This is a more expensive way to provide any given level of property tax relief to homeowners, as some relief bleeds out to non-residential property owners.

Owners of high-priced residential property in a district also often benefit more from rate cuts than homestead relief – as the constitution's limit keeps their homestead relief smaller than what may be attained under a rate cut.

How a four-mill (.004) rate cut in a district with property taxes of 13.3 mills would affect different types of properties is illustrated in Figure 2. In all cases, the rate cut lowers property taxes by 30%. For a low-priced home, the relief reduces its tax bill by $300. For the median-priced home in the district, the rate cut reduces its tax by $600. In both cases, this is far less than would have been received through homestead relief ($1,000 in this example).

For those with homes above the median value in the district, the benefits of a rate cut over homestead relief grow as their home's price increases. In Figure 2, the owner of a house valued at $400,000 receives a tax cut of $1,600 from the rate reduction - $600 more than under the maximum homestead relief. For non-homestead owners, the value of rate cuts over homestead relief are obvious. While the owners of a factory worth $1 million would receive $0 in homestead relief, the rate cut reduces their tax bill by $4,000.

Figure 2.



	Low-Priced Home ($75K)	Median-Priced Home ($150K)	High-Priced Home ($400K)	Factory ($1M)
Before	$1,000	$2,000	$5,333	$13,333
Rate Cut	$300	$600	$1,600	$4,000
After	$700	$1,400	$3,733	$9,333

Source. Pennsylvania Budget and Policy Center

How much non-residential property a school district has, which in 2012 varied from 5.9% in suburban Wallingford-Swarthmore to 91.5% in coal-rich West Greene, will determine how much non-homeowners benefit from a rate cut. On average, 30% of a school district's assessed property is non-residential.[8] This means that $3 of every $10 of rate relief, on average, would go to other types of taxpayers than residential.

Conclusion

When people talk about property taxes, the group most often mentioned is seniors. In most cases, as the examples above indicate, homestead relief would provide greater benefits to seniors than rate cuts: Seniors living in modestly priced housing, with less ability to pay than owners of higher-price housing, would receive greater benefits under homestead relief.

Homes and other properties are a form of wealth. If the goal of providing property tax relief is to safeguard those with the least ability to pay property taxes, it makes sense to provide that relief through the homestead exemption rather than general rate cuts. The restriction of homestead relief to half of the median home's property taxes limits the cost of providing tax relief and does not provide more relief to those with more expensive houses (and greater ability to pay) the way that a rate cut does.

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[8] PBPC review of Pennsylvania Department of Community and Economic Development, Tax Equalization Department (TED) land and use data from 2012, http://www.newpa.com/webfm_send/3507.