What Goes Up Must Come Down

Property Taxes and Tennessee's Truth in Taxation Law

Beacon
CENTER OF TENNESSEE

Key Takeaways

- More and more states are copying Tennessee's Truth in Taxation law, which ***requires local governments to consider a tax rate that won't raise more revenue after property reappraisals***.

- While it does increase transparency, ***"Truth in Taxation" does not prevent tax increases***. Over 30 percent of reappraisals since 2015 have resulted in tax increases over the certified tax rate, the revenue-neutral rate calculated after reappraisals.

- Since 2000, tax rates have fallen just shy of one percent per year, whereas ***property tax revenues have increased an average of more than five percent per year***.

- Tennesseans are susceptible to large property tax increases because the Volunteer State is ***one of only four nationwide without a cap on the growth in property taxes***.

- Tennessee policymakers should consider updating the Truth in Taxation law's disclosure clause to ***require the local governments to send mailers*** to property owners, similar to Utah's law, and ***implement a levy referendum trigger on the growth of property tax revenues***. This would allow revenues from property taxes to grow by a certain percentage per year and allow more to be collected if voter approval is given, similar to Tennessee's wheel taxes.

Introduction

On April 16, 2021, Nashville Mayor John Cooper needlessly created false hope for thousands of Nashville property owners when he went on a media tour starting with "*News Channel 5 This Morning*" and told Amy Williams that the previous 34 percent property tax hike "ends up being reversed" and that people's "taxes are not gonna be going up, it's gonna be coming down because we're able to produce a massive property tax rate cut."[1] The quote and subsequent interviews that day resulted in a media firestorm, with multiple city leaders calling into question the mayor's comments, describing them as "misleading" and saying it was impossible to know what the tax rate would be at that time.[2] The reason: a state law more than 40 years old known as Truth in Taxation prevents higher appraisal values from automatically leading to higher property taxes. Sadly, comments about a law meant to bring clarity and transparency for homeowners brought nothing but confusion and disappointment.

Economists and governments often prefer property taxes because they are a stable source of revenue for localities. Additionally, while many other forms of taxes pick winners and losers, property taxes tend to be economically neutral and come closer to a "user fee" than most other taxes.[3] However, no tax is without its drawbacks. Property taxes have pronounced effects on businesses, as they cannot be written off like other forms of taxation. Studies have even shown that property taxes particularly harm new business and startup rates since they are paid regardless of profit.[4] Additionally, property taxes affect decisions concerning business locations. A 10 percent increase in business property taxes decreases the number of new plants opening in a state by between one and two percent.[5] These negative effects make large property tax increases even more problematic for taxpayers and the state's economy generally. While Nashville's recent 34 percent tax hike is perhaps the most notable, large property tax hikes are a statewide phenomenon. Using 2019 as an example as the last year before the COVID-19 pandemic, the Beacon Center identified more than $208 million in proposed or adopted property tax increases across the state (Figure 3).

The ABCs of CTRs

Every four to six years, Tennessee counties are required to conduct a general property reappraisal.[6] Afterward, a new tax rate is calculated that would provide for the same property tax revenue as the prior year.[7] For example, prior to the recent reappraisal, Nashville's property tax rate was $4.221 per $100 of assessed value for the city's more urban areas. The new revenue neutral tax rate after the reappraisal was $3.2889. This updated rate is known as the "certified tax rate," and the polices for calculating it are

1 Laken Bowles, "Mayor John Cooper announces property tax rate cut for Nashville as overall property values rise." *News Channel 5 Nashville*. April 16, 2021. https://www.newschannel5.com/news/mayor-john-cooper-announces-property-tax-cut-for-nashville-34-increase-will-be-reversed.
2 Ibid.
3 Bruce Walin and Jeffrey Zabel, "Property Tax Limitations and Local Fiscal Conditions: The Impact of Proposition 2 1⁄2 in Massachusetts." Lincoln Institute of Land Policy Working Paper. 2010. https://www.lincolninst. edu/sites/default/files/pubfiles/1885_1200_wallin_zabel_wp11bw1.pdf.
4 Timothy J. Bartik, "Small Business Start-Ups in the United States: Estimates of Characteristics of States." Southern Economic Journal. April 1989. https://www.jstor.org/stable/1059479?origin=crossref&seq=1#page_scan_tab_ contents.
5 Timothy Bartik, "Business Location Decisions in the United States: Estimates of the Effects of Unionization, Taxes, and Other Characteristics of States." *Journal of Business and Economics Statistics* 3:1 (January 1985): 14–22.
6 Tenn. Code Annotated §67-5-1601(a).
7 Tenn. Code Annotated §67-5-1701(a)(3).

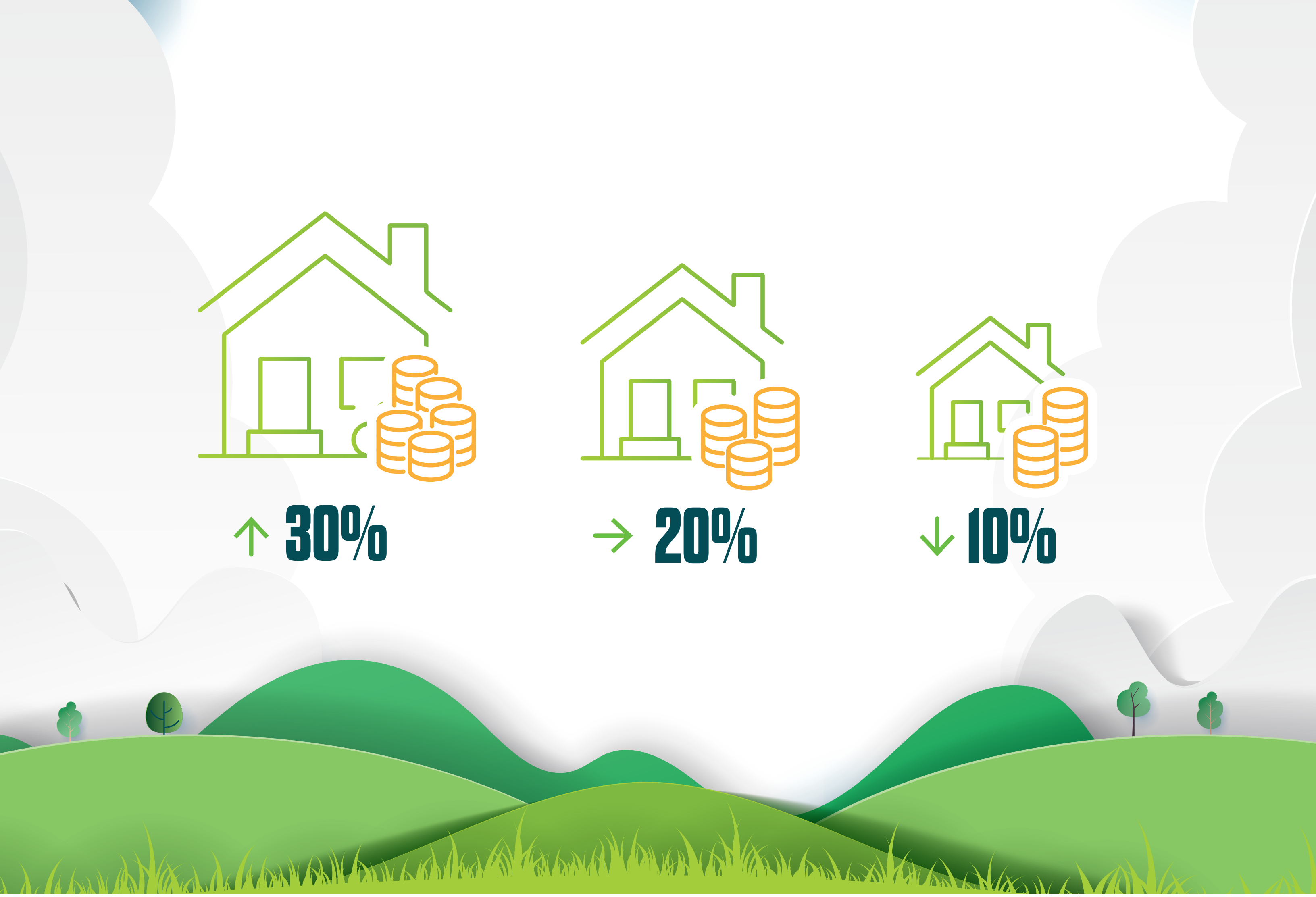

Figure 1: In the above example where average property values went up 20 percent, properties that appreciated more than average will pay more in property taxes and vice versa, while the total revenue collected will remain the same.

created by the State Board of Equalization.[8] Similar to a cap on assessment limits, the certified tax rate prevents local governments from receiving a windfall of new revenue from taxpayers just because home values have risen.

Additionally, because the certified tax rate is based on the total revenue collected from property taxes, individual property owners may still receive a different tax bill. If one's property appreciated more than the county average, that property owner's taxes will go up. Meanwhile, homeowners whose property appreciated less than the average can expect to pay lower taxes as a result of the reappraisal (Figure 1).

However, it is important to note that cities and counties may choose to adopt a tax rate that is higher than the certified tax rate, thereby raising overall taxes. If the locality wishes to adopt a new tax rate higher than the certified tax rate, it must place an ad in a local newspaper, send an affidavit to the State Board of Equalization documenting the ad's publication, and then adopt the new higher tax rate at a public hearing.[9]

8 Tenn. Code Annotated §67-5-1701(b)(1).
9 Tenn. Code Annotated §67-5-1702.

Truth in Taxation Is Trendy

While Tennessee was the first state in the country to have this level of transparency for property taxes on the books, it is not the only one. In 1985, Utah also passed a Truth in Taxation law after years of rapidly increasing property values and concerns over transparency. The effort worked. In the 10 years before Utah's law passed, revenues increased 12 percent annually. In the decade after its passage, revenues increased four percent annually.[10] However, Utah's version differs in one key way: Utah localities must meet the disclosure requirements for *every* proposed tax increase. Utah cities and counties must place the notice in two newspaper articles and must mail notifications to each parcel owner outlining the value, current tax, proposed tax rate, location, and the date and time of the hearing.[11]

Recently, the Truth in Taxation model has become increasingly popular. Earlier this year Kansas, where average property tax increases have been 2.8 times greater than inflation plus population growth, became the third state to implement this law.[12] Nebraska also implemented just the disclosure part of the Truth in Taxation process this year, requiring local governments to notify taxpayers whenever their property taxes are scheduled to increase more than two percent.[13]

The Truth About Truth in Taxation

The reason more states are looking to the model originally implemented here in Tennessee is that it does help keep property tax burdens down, with some calling it the "gold standard of property tax legislation."[14] Since 2008, Tennessee's property tax burden has always been in the bottom 10.[15]

However, while it does prevent an *automatic* windfall of new revenue, data shows that the law does not serve as an effective limitation on property tax increases, even in reappraisal years. Using historical data from the Comptroller's Office of certified tax rates and adopted tax rates back to 2015, we see that counties have been willing to raise taxes above the certified tax rate during reappraisal years roughly one-third of the time.

County Responses to New Certified Tax Rates

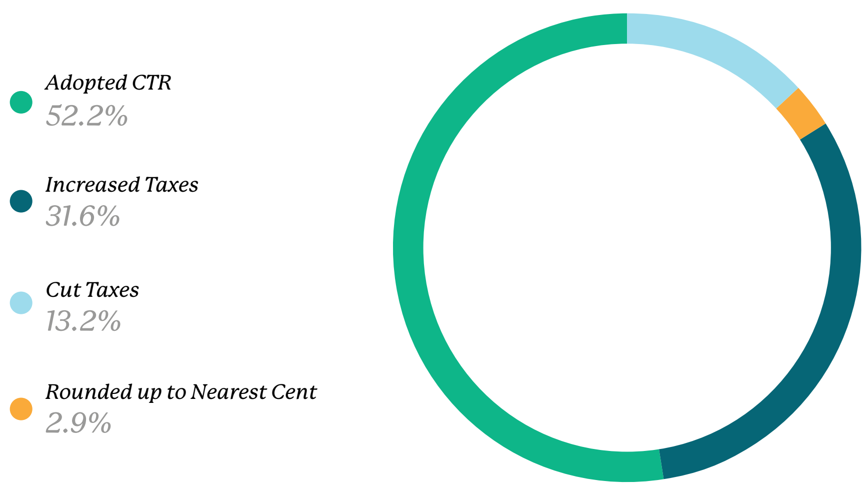

Figure 2: Historical data shows that counties are willing to deviate from the certified tax rate roughly 50 percent of the time, with the majority of those cases coming from tax increases.

10 Christopher Collard and Christian Mickelsen, "The Essential Tax: Property Taxation in Utah." Utah Foundation. February 2018. https://www.utahfoundation.org/wp-content/uploads/rr750.pdf.
11 Ibid.
12 Dave Trabert, "Gov. Kelly signs property tax transparency bill." Kansas Policy Institute. March 31, 2021. https://kansaspolicy.org/gov-kelly-signs-property-tax-transparency-bill/.
13 Taylor Gage and Justin Pinkerman, "Gov. Rickett Calls 2021 Legislative Session 'Historic.'" May 28, 2021. https://governor.nebraska.gov/press/gov-ricketts-calls-2021-legislative-session-%E2%80%9Chistoric%E2%80%9D.
14 Jonathan Williams, John Hendrickson, and Lee Schalk, "Truth-in-Taxation Laws Are Gold Standard of Property Tax Reform." *The Daily Signal*. April 29, 2021. https://www.dailysignal.com/2021/04/29/truth-in-taxation-laws-are-gold-standard-of-property-tax-reform/.
15 "Rich States Poor States: Tennessee." American Legislative Exchange Council. https://www.richstatespoorstates.org/states/TN/.

Cities and Counties in Tennessee with Proposed Tax Hikes in 2019

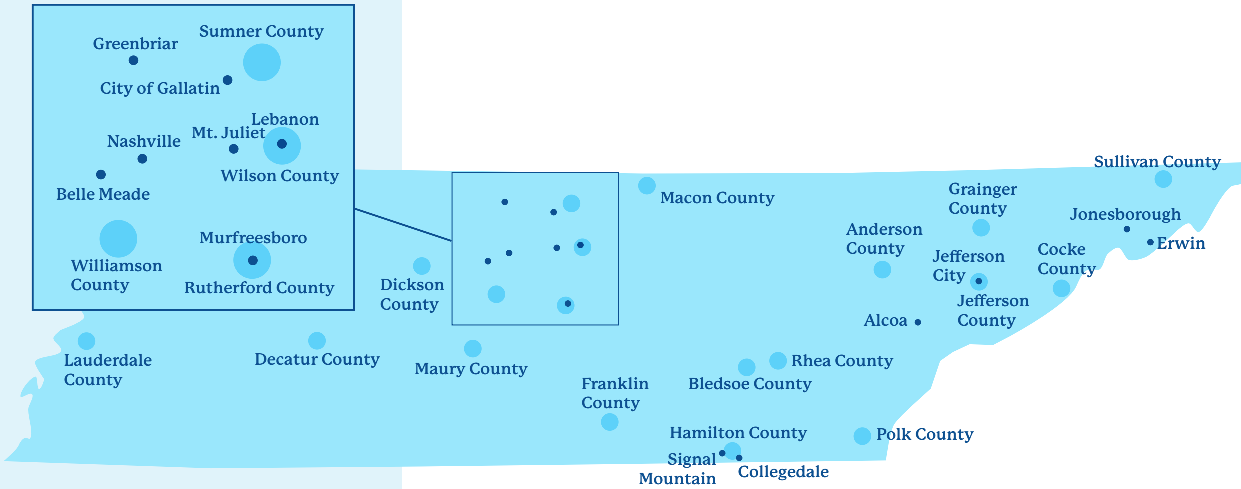

Figure 3: Proposed property tax increases do not fit any real trend, with both cities and counties in both urban and rural areas proposing them.

When local governments institute a tax hike in a reappraisal year, voters may get confused, if not outright misled—as was the case this year in Nashville. Local governments may focus on how the tax rate is decreasing while revenues collected or even taxes assessed could be going up. For example, in 2019 the city of Murfreesboro highlighted the fact that its tax rate was 50 percent less than in 1999 while proposing a massive tax increase.[16] That same year, one commissioner in Anderson County highlighted that after supporting a tax increase, the tax rate would still be less than the rate it had been when he moved there 40 years earlier.[17]

Truth in Taxation clearly does little to protect taxpayers from property tax hikes in reappraisal years; it also does nothing to protect them in non-reappraisal years. Nor has it prevented local governments from collecting increased revenues from property taxes. The Beacon Center pulled historical property tax revenue and rates from a sample of cities and counties across the state back to at least 2010.[18] While rates have fallen an average of 13 percent since 2000, property tax revenues have continued to climb, up an average 5.4 percent per year (3.7 percent annually if one excludes years in which a tax hike occurred, essentially capturing "growth only" years).[19]

Rutherford County and Murfreesboro, for example, jointly passed a 40 percent increase on their residents in 2019. The reason Tennessee taxpayers are at more risk to these large increases is because Tennessee is one of the few states without a statewide property tax cap despite being the first state with a Truth in Taxation law.

Take It to the Limit—If There Is One

Tennessee is only one of four states in the union that does not have a state-imposed limitation on the growth of property taxes. Hawaii, New Hampshire, and Vermont join Tennessee as lacking any of these limitations.[20] These states are not exactly the company Tennessee wants to keep.

16 Michelle Willard, "Murfreesboro takes to social media to spin tax hike, commenters not impressed." *Murfreesboro Voice*. June 5, 2019. https://www.murfreesborovoice.com/article/2656/murfreesboro-takes-to-social-media-to-spin-tax-hike-commenters-not-impressed.
17 Ben Pounds, "Property tax bills going up." *Oakridger*. August 16, 2019. https://www.oakridger.com/news/20190816/property-tax-bills-going-up.
18 The Comptroller of the Treasury maintains the history of tax rates since 1997 and Comprehensive Annual Financial Reports to at least 2010, some since 2000.
19 Local governments included: Anderson County, Chattanooga, Clarksville, Crossville, Cumberland County Franklin, Hamilton County, Hancock County, Johnson County, Knox County, Knoxville, Lake County, Memphis, Montgomery County, Murfreesboro, Nashville, Pickett County, Rutherford County, Shelby County, Sumner County, Williamson County, and Van Buren County.
20 Jared Walczak, "Property Tax Limitation Regimes: A Primer." The Tax Foundation. April 23, 2018. https://taxfoundation.org/property-tax-limitation-regimes-primer/.

There are generally three types of statewide caps on property taxes: assessment caps, rate caps, and levy caps. Assessment limits seek to accomplish similar results to Truth in Taxation. The idea is to prevent someone from being priced out of their home by capping assessment increases entirely or by some amount (say five percent per year, for example). The downside of an assessment cap is that it can lead to inequalities over time, punishing younger and newer homeowners and "locking" residents into their homes as sales or transfers lead to a reassessment. California has one of the most restrictive and well-known assessment caps, known as "Prop 13"—only allowing assessments to raise two percent or the rate of inflation, whichever is less. If a local government wishes to raise property taxes by any

States with Limitations on the Growth of Property Taxes

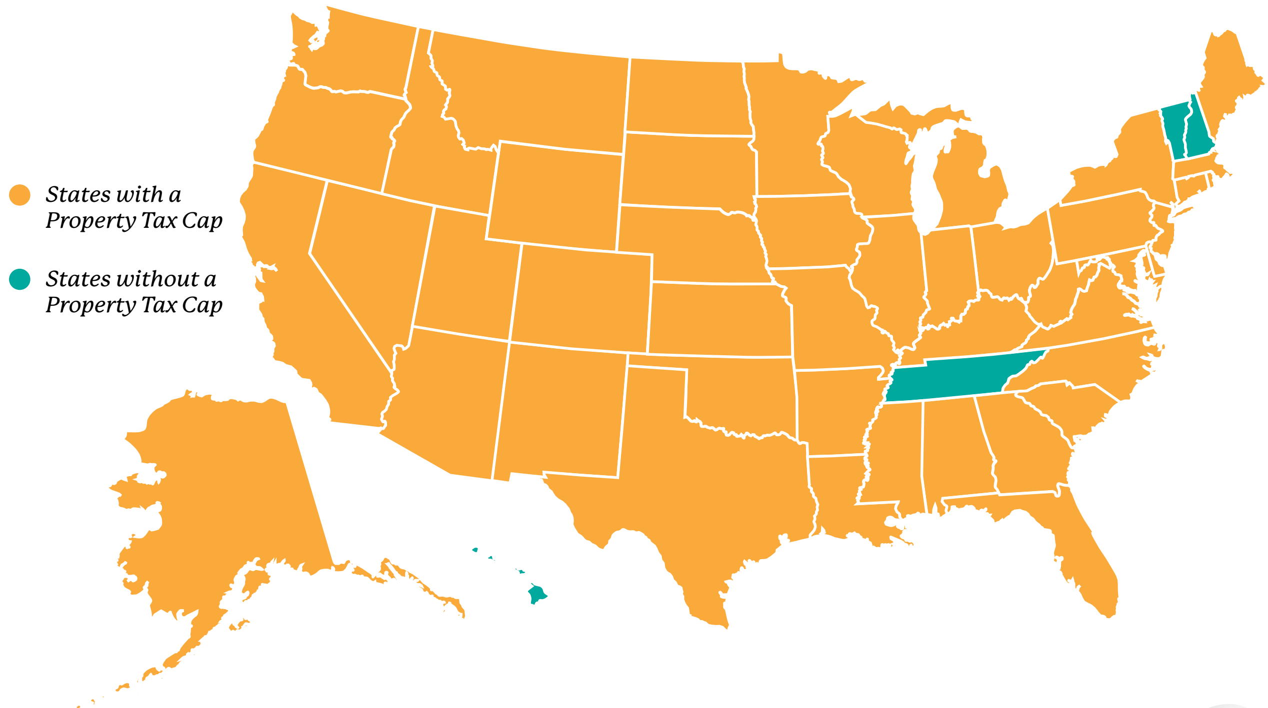

Figure 4: In what may be a surprise to many, Tennessee is an outlier by not providing this basic protection to taxpayers.

amount above two percent or inflation, an election must be held and the decision is left to the voters.[21]

Rate caps—the simplest form of a property tax cap—simply limit the percentage increase of the millage rate and serve as a policy restriction on local governments from adopting a tax increase. A rate cap could freeze rates altogether, allow them to increase by a set amount, or impose a rate ceiling. This is already the case in Nashville, where a 2006 amendment to Metro's charter capped the city's Urban Services District property tax rate at $4.69 per $100 of assessed value. A public referendum is required to raise it above that figure.[22] One note is that Utah, even with its Truth in Taxation law, also has a maximum rate that counties may impose.[23]

Finally, a levy cap limits the total amount of revenue a local government can collect in any given year. Under a levy limit, while the total revenue collected remains the same, individual property owners may experience a change in their taxes as rates or assessments change. According to the Tax Foundation, "levy limits impose a hard constraint on revenue growth, and have the same revenue effects as imposing both a rate and an assessment limit in concert, though without the inequities and distortions associated with assessment limits."[24] Some notable examples include Alaska's $1,500 limit for each person residing in the municipal boundary or Massachusetts' 2.5 percent revenue growth cap per year.[25]

All three types of limits provide some protection for taxpayers, yet none independently provide complete protections for them. Limits on assessments allow governments to raise rates and increase their revenues, limits on rates do not account for rising property values, and limits on revenue do not restrict local governments from setting independent rates as long as the amount of growth is modest. That is why multiple states impose more than one limit. Thirteen states have only one limit; 25 states have two; and eight (not including the District of Columbia) impose all three limitations. Tennessee should join the vast majority of states in imposing some limit on property taxes to protect citizens from unjust tax increases. While Tennessee's certified tax rate is a good step for transparency—and in theory, if local governments had to accept the CTR, it would act as a levy limit. However, as we have seen, it does not serve as an effective protection from higher property taxes.

During the 2020 legislative session, a bill was introduced that would have provided that extra layer of protection for Tennessee taxpayers. This bill limited the increase of revenue from property taxes to two percent plus inflation, but could be increased more with voter approval.[26] Local governments quickly came out against the plan, calling it "state intrusion" and overreach.[27] But a quick glance around the nation shows this is already the norm, with many states imposing more restrictive limitations in order to protect taxpayers. What is even more unfortunate is that many of these increases are heralded by government leaders as ways to fund core services. Yet as the Beacon Center has pointed out, shortly after tax increases are passed, local governments quickly find ways to spend those dollars on less-than-needed services, such as Rutherford County raising property taxes, then handing over nearly $1 million to Costco.[28]

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21 "Proposition 13 and Real Property Assessments." Sacramento County Assessor. https://assessor.saccounty.net/TopicsAtoZ/Pages/Prop13andRealPropertyAssessment.aspx.
22 Yihyun Jeong, "Koch supported group submits petition to roll back Nashville's property tax increase." *The Tennessean*. August 26, 2020. https://www.tennessean.com/story/news/politics/2020/08/26/nashville-property- tax-hike-opposed-koch-supported-group/3443757001/.
23 Utah Code Annotated 59-2-908(1).
24 Jared Walczak, "Property Tax Limitation Regimes: A Primer." The Tax Foundation. April 23, 2018. https://taxfoundation.org/property-tax-limitation-regimes-primer/.
25 AS 29.45.090(b)(1); "Proposition 2 ½ Explained." City of Gardner, Massachusetts. https://www.gardner-ma.gov/DocumentCenter/View/2768/Proposition-2-12.
26 Yihyun Jeong, "Tennessee lawmaker sponsors bill putting cap on property tax hikes." *The Tennessean*. January 22, 2020. https://www.tennessean.com/story/news/politics/2020/01/22/tennessee-lawmaker-sponsors-bill-putting-cap-property-tax-hikes/4531953002/.
27 Yihyun Jeong, "Tennessee mayors call proposed property tax cap 'state intrusion'." *The Tennessean*. January 26, 2020. https://www.tennessean.com/story/news/politics/2020/01/27/tennessee-property-tax-bill-mike-bell/4564363002/.
28 "2019 Tennessee Pork Report." Beacon Center of Tennessee. December 11, 2019. https://www.beacontn.org/wp-content/uploads/2019/12/BCN_PorkReport2019_WEB-1.pdf.

Conclusion & Recommendations:

The Final Pieces of the Puzzle

As we have witnessed with Nashville Mayor Cooper's recent faux pas, a misunderstanding of the state's Truth in Taxation law can at best create confusion among taxpayers, or at worst, be used to deceive them. Additionally, while the law does prevent Tennesseans from *automatically* paying higher property taxes, it has clearly provided little defense against property tax hikes. In essence, the law serves mostly as a transparency vehicle, requiring voter notification if a local government wishes to adopt a rate higher than the certified tax rate. However, a lack of understanding can create confusion around a law intended to better inform taxpayers. This is especially true as the law's required method of notification to taxpayers, through a newspaper, becomes an increasingly outdated medium of communication. In order to better inform taxpayers and bring clarity to the Truth in Taxation law, Tennessee lawmakers follow Utah's model by requiring notices to be mailed out to taxpayers.

Finally, Tennessee is in dire need of some form of additional protection for property owners. Without some form of modest limitation, Tennesseans will continue to be vulnerable to massive one-time tax increases. Without a property tax limitation, higher property taxes threaten to erode the state-level policies that have made Tennessee competitive and attractive for workers and businesses alike, such as our lack of a state income tax, the repeal of the Hall Income and death taxes, and our right-to-work status. As other states continue to make themselves more competitive, Tennessee cannot rest on its laurels if we want to continue to grow into an economic powerhouse. A property tax cap like those in 46 other states, when paired with our existing Truth in Taxation law, would ensure that all of our state's policies are competitive and create the nation's strongest economic environment.

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