Analysis of a Proposed Real Estate Transfer Tax for the State of Louisiana

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Executive Summary

A real estate transfer tax (RETT) is a tax imposed on the transfer of real estate in order to add to a state's general revenue or to fund a particular program. This report describes the unfairness of such a tax.

Specifically, the tax is regressive, imposes a large burden on a small segment of taxpayers who do not benefit from a proposed use, and is more volatile than the general economy. The RETT can limit housing affordability for thousands of moderate-income households, particularly first-time homebuyers and those who want to move for economic opportunity.

The RETT is a poor choice of taxation. It does not provide a consistent source of revenue and has negative implications for providing affordable housing, especially for those of moderate income.

Introduction

With the national economy in recession, state and local governments' search for new funding sources has taken on special urgency. In this context, the multi-billion-dollar market for real property presents a tempting target, promising significant funds even at relatively low tax rates. Most local governments already impose taxes on real estate transactions, requiring, at a minimum, a fee whenever a property deed is recorded. In most cases, this is a nominal amount commensurate with the costs of maintaining the system of public records. Some jurisdictions have turned the fee into a value-based tax intended to raise revenues. In addition, a majority of the states that tap into this process do so to add to the general revenues or to fund specific dedicated accounts.

Currently, the state of Louisiana is not among these states. The Louisiana Housing Finance Agency, which administers the state's Housing Trust Fund, has publicized its interest in such a tax to fund subsidized housing production. The National Association of Realtors (NAR) has stated its opposition to the proliferation of these real estate transfer taxes, largely because of their negative impact on real property markets and the unfairness of such a narrow-based tax. This report focuses on the arguments against employing a tax on real estate transfers within a Louisiana context.

Real Estate Transfer Taxes (RETTs)

Local governments maintain a public records system so that the chain of ownership for any given real property is public information. The system is instrumental in the ability of sellers to deliver clear title when a property is sold. Most jurisdictions require a fee to record a document commensurate with the costs of maintaining the system. Typically such fees add less than $100 to transaction costs when a single-family home is sold.

In some cases, an enlarged fee may be assessed on each transaction, the proceeds of which go into the general fund. A true RETT takes the form of a **fee equal to a percentage of the sales price or value** of the property transferred (some localities tax mortgages, as well). State government must provide authorization for local governments to collect such a tax. Quite often, the state collects the tax itself and keeps the revenues. It is not unusual for a tax to be assessed by both state and local governments. Table A-1 in the appendix indicates the range of rates applied to these taxes across the country.

Normally, the cost of deed recording is placed on the buyer. The transfer tax may be required of seller or buyer, or both, depending on the jurisdiction. The parties to any transaction may effectively reassign these costs when negotiating the terms of sale.

The RETT is relatively simple to assess and collect. Tying payment to the recording process minimizes tax evasion, since an unrecorded deed forfeits the full legal protections afforded legitimate ownership and would preclude standard mortgage financing. The largest issue would be validating the sales price when that is used as the basis for the tax.

The popularity of the RETT (among state governments) is attested to by the number of states that have imposed it. At the same time, the RETT rate is relatively low in all but a handful of states. Since the rate applies to the full sales price of the property, rather than to the sales profits or owner's equity, even a low rate may impose a large amount of tax. The canvas of states reflected Table A-1 in the appendix was made in 2005, long before the widespread revenue shortfalls of recent years. With revenues from traditional sources shrinking, pressure on the remaining states to find new sources will only intensify. If not for its own purposes, states can authorize local governments to impose RETTs as a way to relieve demands on state assistance. This was the case in North Carolina, where in 2007 the state offered tax authorization in exchange for the locals taking over part of the costs of Medicaid (the legislature added a requirement for public approval of the tax in each jurisdiction, although the referendums failed in all of the 16 counties putting it to the vote).

The RETT is a common device, as well, to finance accounts dedicated to specific purposes; such as provision of affordable housing or environmental amenities. Perhaps the connection of housing and environment to real estate seems to justify the tax in the view of its advocates. According to the Center for Community Change, 10 states currently use the transfer tax to provide revenues for a housing trust–type agency intended to produce low-cost housing. An examination of tax equity shows little or no justification for placing such a burden on real estate purchasers.

NAR Concerns

As mentioned earlier, the NAR has publically stated its opposition to the proliferation of RETTs and urges its state affiliates to work to defeat newly proposed extensions. Its concerns include:

- **Expected and demonstrated deleterious effects on the real estate market**, particularly the housing market. RETTs, at significant levels, tend to depress both market activity and prices, interfering with families' ability to move and renters' ability to become homeowners.
- **Fairness of the tax.** Targeting only those who buy and sell real estate places a burden on a small group to provide for benefits for the general citizenry. Like other sales taxes, the RETT places a more significant burden on lower-income taxpayers compared to those who are more affluent. Some observers feel there is an implicit bargain between government and property owners to exempt real property from transaction taxes in exchange for an annual property tax. The RETT represents a reneging on that bargain.
- **Reliability as a revenue source.** The narrowness of the tax base makes RETT revenues potentially volatile. For example, revenues from the Pennsylvania RETT were down 31% in

the latest fiscal year. General tax revenues were off only 7.3%. Proceeds from a similar tax in Washington State were down over 40%, compared to an 8% drop in overall tax revenue. Real estate markets have been especially hard hit by the recession and taxes based on market activity could suffer further declines.

- **Tax avoidance.** The tax, if significant, could influence the decisions of homeowners and businesses to locate within the state. The effect would be felt mainly at the borders, where the economic base of Louisiana cities spills over into adjoining states. Specifically, this could be an issue for Shreveport (Texas), Lake Charles (Texas), and New Orleans (Mississippi).
- **Housing affordability.** Formidable barriers face those attempting to buy their first home. These include affordable financing, accumulating a down payment, and finding cash for the substantial transaction costs associated with most home sales. The RETT can increase these costs to a significant degree. Many regard homeownership as desirable, benefiting society through increased social stability and commitment to the community.

These concerns will be discussed and documented through the remainder of this report.

Who Pays the Tax?

The legal responsibility for paying the tax does not necessarily determine who ends up bearing the burden of the RETT. The "**incidence**" of the tax may be shifted to a party other than the actual payer. In a negotiated sale, any costs incurred in the transaction can be effectively reallocated by mutual consent. Over time, recurring and predictable costs will be reflected in the price of the traded property. Thus, a cost that is imposed by law on the buyer may be shifted to the seller in the form of a price discount.

When a tax applies uniformly to all producers, it may shift the supply curve. Likewise, a uniform tax on all consumers shifts the demand curve. In either case, the tax will change the market price of the product. A tax that is incurred by only some sellers or buyers would have to be absorbed by those sellers or buyers in a competitive market. For example, if the tax fell only on home sales in certain neighborhoods, those sellers would have difficulty shifting the tax incidence, since sellers in untaxed areas could offer comparable houses at lower prices. Given uniformity in application, shifting of the RETT burden depends on how much bargaining power sellers have relative to buyers. In a "sellers' market" (strong demand and insufficient supply), most of the costs could be shifted to the buyer. A "buyers' market" (weak demand and much supply) would result in the opposite shift.

Is it important whether the buyer or seller is charged with the tax? In a perfect market, perhaps not. However, there are some institutional factors that do affect the choice. If the tax is paid by the buyer, it comes out of the cash resources of the buyer. When mortgage loans were easy to come by, borrowers could push a significant amount of closing costs into the loan and spread the costs over the term of the mortgage. That ploy is no longer possible under today's tightened loan criteria. A RETT falling on buyers would significantly reduce demand from cash-challenged buyers. If the tax is paid by the seller, it could be shifted by raising the sales price and, if this practice became the market norm, prices would rise to reflect the tax. The buyer then could finance as much of the shifted tax as the appraisal would allow. Thus, there is a slight bias toward allocating RETT payment to the seller in exchange for a higher price. At the same time, any shifting will depend on whether buyers or sellers hold the upper hand in negotiations, which in turn depends on economic conditions in the current market.

One study provides evidence of full capitalization of seller concessions (sellers agreeing to pay costs normally born by buyers) into sales prices. In other words, sellers were able to raise their prices to capture the concessions. In fact, prices for entry-level homes included a “liquidity premium” 30% above the amount of the concessions, reflecting the enhanced value of these concessions to cash-strapped first-time buyers. However, it should be noted that the study was conducted in 2007, when a strong sellers’ market was in effect.

Tax Equity

Equity is the way economists measure how fairly a tax affects taxpayers. In general, a tax is considered fair if it satisfies two criteria of equity:

- **Tax burden commensurate with benefits derived**. Those who benefit from the services provided by the tax should pay an amount commensurate with those benefits.
- **Tax burden commensurate with ability to pay**. The tax burden should be in relation to one’s ability to pay. Ability to pay can be related to the amount of discretionary income the taxpayer has or to the amount of liquid assets available to pay the tax.

No tax can be completely fair, but, as public policy, a tax should be designed to maximize equity while achieving its primary purpose—to raise revenue. In this regard, the RETT fails the equity criteria in both matching benefits derived and in ability to pay.

Benefits

A tax that pays for **benefits that accrue to the taxpayers** is considered equitable. For example, a user fee for those who use a public marina is considered fair since the users get the most benefit. A deed recording fee is equitable because it pays to sustain a system for securing property title. Also, a tax that clearly benefits those who pay the tax would have no effect on demand and not reduce property values. For example, a local government that charges higher property taxes to provide better public schools may actually boost the value of homes in the jurisdiction because superior schools are highly valued by taxpayers.

The proceeds of RETTs are either combined into the general fund or dedicated to special-purpose accounts. In the former case, tax proceeds go toward government services in general. The latter usually provide funds to subsidize housing for lower-income residents or to purchase open space and environmentally sensitive land (in Louisiana, the most likely proposal is that it would be used for low-income housing projects). These uses may be very beneficial to the public, but neither is of benefit specifically to those bearing the tax. It would be unfair to burden this group alone with a tax that provides them no particular benefits.

The **tax base** for the RETT is extremely **narrow**. Less than 4% of the households in Louisiana buy a home each year, and a much smaller percentage are involved in other real estate sales (land, commercial buildings, apartment projects). Yet this small minority is expected to pay taxes for services that benefit everyone. If the proceeds are used to subsidize homes for selected families, it will come at the expense of other families who will have difficulty buying a home because of the tax. Advocates of state housing trust funds claim that every dollar of funding generates $5 to $10 of economic activity, a benefit that is not specifically enjoyed by the ones affected by the tax. More than half of the projects sponsored by the Louisiana Housing Finance Agency are rental housing, according to its latest housing trust fund report (October 2009). It is hard to see how current homebuyers derive any special benefits from more subsidized apartments.

Since the RETT falls only on those who buy and sell property, the burden is not one that affects all property owners. An economic case can be made that taxes on property value are justified since the government services and activities they fund indirectly enhance those values. No such connection can be made to a tax on title transfers, especially when that tax is applied in addition to property taxes.

Impact fees are imposed in many jurisdictions when developers propose a new residential subdivision. The purpose of impact fees is to offset the added cost of public services represented by the new housing. The fees may be imposed to pay for improvements to roads, water and sewer facilities, libraries, parks, or fire and police facilities. The added expense of the fees ends up raising the price of the homes, but the municipality uses the impact fee to help make new development pay its own way rather than impose extra costs on existing residents. Thus, the tax must be justified by demonstrating that the area that benefits from added public services corresponds with where the tax is imposed and that impact fee proceeds are not used to enhance services for incumbent residents. Since a RETT applies to all who buy or sell a property, it does not meet any of these service tests.

Progressivity

The popular appeal of Robin Hood's "taking from the rich to give to the poor" rests on the perception that the higher one's income, the more one can spend on things other than the necessities of life. Therefore, one can shoulder a higher percentage of the costs of public benefits without undue hardship. A tax designed to do this is termed "**progressive**," since the percentage of tax on income increases with income. If the tax rate increases as income declines, the tax is termed "**regressive**." While some might debate whether a progressive tax is more fair than a proportional tax schedule, no one would consider a regressive tax equitable.

As an example of a regressive tax, consider a sales tax applied to a loaf of bread. A low-income person pays the same rate and amount of tax as a wealthy person, but the tax is disproportionately high compared to the low-income person's income or wealth. That is why many jurisdictions exempt food necessities from sales taxes. Catered and restaurant meals are not exempt, as they are considered luxuries.

A RETT is similar to a sales tax on food. Housing, as a necessity, requires a larger portion of a low-income person's budget. Therefore, it is a heavier burden as income declines.

At first glance, the RETT might appear to be progressive, since the amount of tax is in proportion to the value of the property, and that value should increase with the income of the owner. However, for a tax to be progressive, the tax amount **relative to income** would have to increase with income. While people generally buy more expensive houses as their income increases, the value does not increase as fast as income (which is true of most non-luxury items and is why the rich tend to have more discretionary income).

The progressivity of a tax can be measured by calculating an **effective tax rate**—the tax burden as a percentage of income—for various income brackets. A RETT usually is applied to all types of property. For property not used as a primary residence by the owner (income and investment property), it is impractical to do this calculation, since the buyer's income has no relation to the property value. If it is assumed that the homebuyer incurs the tax burden, it is a simple matter to calculate effective tax rates for owner-occupied residential property. Data on the relationship between home value and homeowner income are readily available.

Regressivity

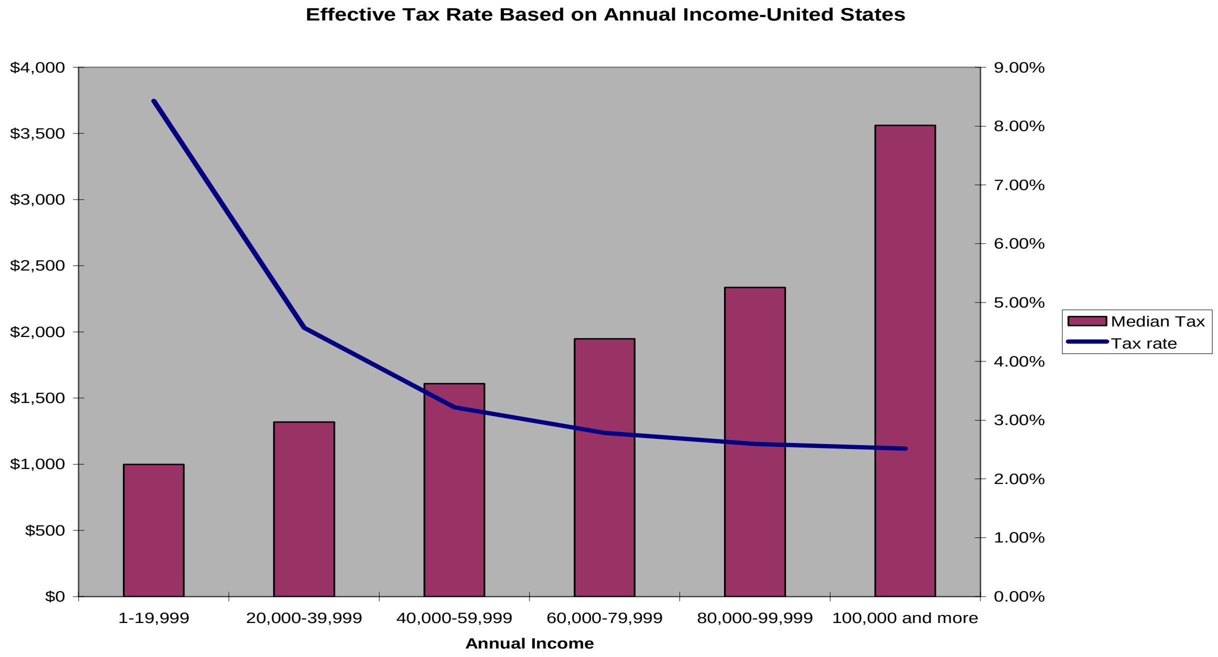
Figure 1 shows effective rates, based on a RETT equal to 1% of value, for homeowners at various income groups nationally. The effective tax rate as a percentage of total income is shown by the blue line and is read from the right-hand scale. A local version of the same data is shown in Figure 2, based on the metropolitan area of New Orleans (the data used to produce this table are not reported at the state level). Both sets of calculations indicate the **strong regressive nature** of the tax, in that the effective rate declines as income rises. The tax rate for the lowest income group is about three times that of the highest group. Although the median tax amount paid rises with income (shown in the columns on the chart), the amount does not rise as fast as income. This pattern reflects the necessity of low-income families to spend a large proportion of their income to purchase a home.

Since few households buy a home every year, it might be more appropriate to calculate the effective tax rate relative to the income earned during the entire time they live in the home. After all, it could be argued that the taxpayer has all that time to accumulate the funds for the transaction. Measuring the tax in this way may mute the regressive nature of the tax for, while lower-income homeowners pay a larger percentage of income for housing, they also tend to move less frequently. Such a **tenure tax rate** can be estimated based on the average time between moves for homeowners within the various income brackets. The tenure tax rates for the nation, based on a 1% transfer tax, are shown in Figure 3. As can be seen, the tax remains significantly regressive. The rate on the lowest incomes is more than twice that on the highest.

The regressive nature of the tax is emphasized by the realization that real property, in the form of a home, is a more prominent component of the net worth of a lower-income household. As income rises, households are more likely to hold financial assets, such as stocks and mutual funds, in addition to owning a home. Such financial assets generally do not incur a transaction tax. The regressive feature of such a discriminatory tax are displayed in Table 1 by how the **tax burden of a RETT increases as total wealth declines.**

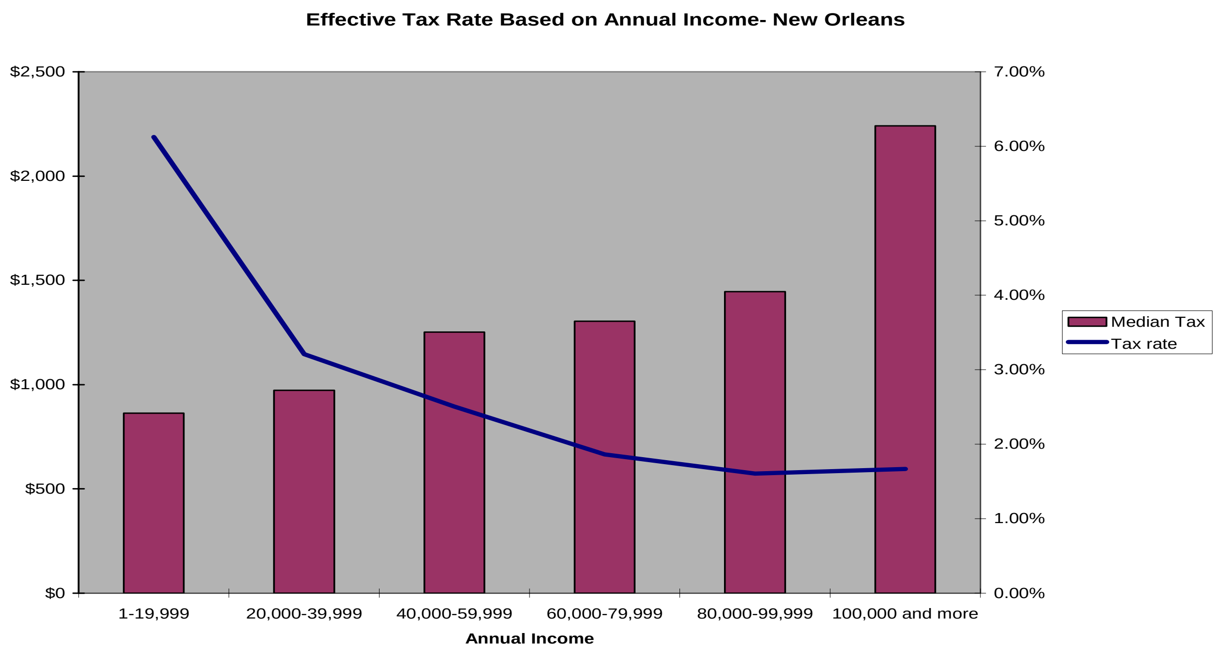
A few states attempt to make the RETT more progressive through the use of tax rates that increase with the value of the property (see Table A-1 in the appendix). Another possible approach would be to offer a credit on the state income tax to taxpayers below a specified income level equal to all or a portion of any transfer tax paid by the taxpayer. While these measures may make the tax less regressive, they also have the effect of making the tax burden more disproportionate with benefits derived and more complex.

Figure 1



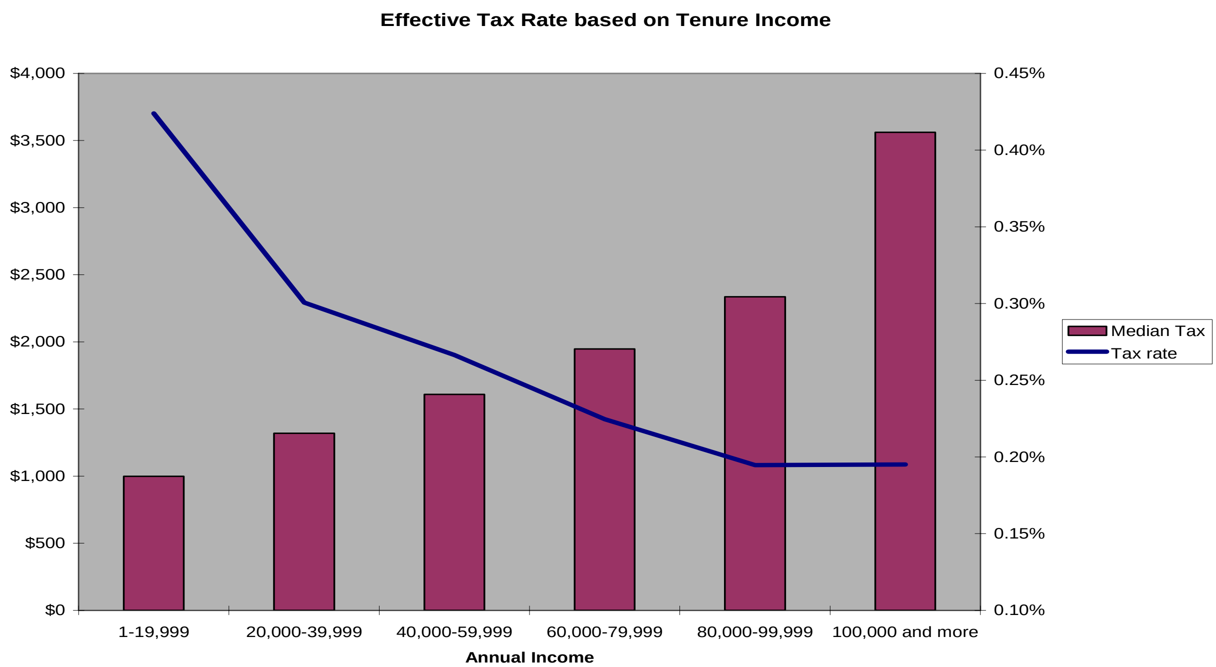
Source: Derived from data reported in the *American Housing Survey*, *2007*, U.S. Census Bureau.

Figure 2



Source: Derived from data reported in *American Housing Survey: New Orleans*, *2004*, U.S. Census Bureau.

Figure 3



Source: Derived from data reported in the *American Housing Survey, 2007*, U.S. Census Bureau.

Table 1

Real Estate Transfer Tax (1 percent) Compared to Total Household Assets
United States, 2007

Income	Median Value Principal Residence	Amount of Tax	Median Value Total Household Assets	Tax as % of Total Assets
All households	$200,000	$2,000	$221,300	0.9
Under $20,000	$100,000	$1,000	$23,500	4.3
$20,000–$39,999	$120,000	$1,200	$84,900	1.4
$40,000–$59,999	$150,000	$1,500	$183,500	0.8
$60,000–$79,999	$215,000	$2,150	$342,800	0.6
$80,000–$89,999	$300,000	$3,000	$558,100	0.5
$90,000–$99,999	$500,000	$5,000	$1,358,400	0.4

Source: Federal Reserve Board, *Survey of Consumer Finances.*

Ability to Pay

A concept related to tax equity concerns the ability of the taxpayer to raise the cash necessary to pay the tax. A RETT appears to comply with this criterion since any sale would usually involve some cash. However, real estate sales require a **substantial amount of cash expenses** even before considering an additional tax. As a result of adding to this burden, existing homeowners seeking to move, upgrade, or downsize might have insufficient funds to permit the purchase of a replacement home. First-time buyers would be especially constrained, as accumulating sufficient cash is an important hurdle for most initial buyers.

When the tax is imposed on or shifted to the seller, the negative aspects of this proposed tax may be more pronounced. Often, home sellers are also home buyers, upgrading or downsizing as family situations change or their financial situations dictate. They may need to relocate to find a new job or business because of economic weakness in their present locality. Such mobility is important to national economic stability.

Because of the depressed housing market in which they are selling, proceeds are meager, and sellers need all the resources they can muster to relocate (sometimes after a lengthy spell of unemployment) and purchase a replacement home. There is a strong possibility that housing will be more expensive in the new location compared to where they are leaving. Since such a seller is likely to be in a weak negotiating position both on the sales side and on the repurchase side, the seller probably would end up bearing the costs of any RETTs on either side of the move.

Many households would simply be unable to raise the additional cash. The effect is even more severe under the tighter lending scrutiny of the post–subprime mortgage era. A significant RETT could make **homeownership less widespread**. It is believed that "tenure choice" (the decision to become a homeowner) is based on the "real user costs" of purchasing and maintaining a home. A RETT could increase those costs beyond what many could bear. Bankrate.com estimates that getting a $200,000 mortgage in Louisiana requires $3,042 in closing costs. If that loan were used to buy a $250,000 home, a 1% RETT would add $2,500 to the costs, an increase of 82%.

Alternative Tax Sources

If additional revenues are needed at the state level, there are two broad-based taxes that might be more appropriate sources for services that benefit Louisiana citizens in general. The state income tax is progressive and can raise large amounts of revenue with relatively small rate adjustments. Based on 2008 collections, an increase of approximately 7% in income tax revenues would match those expected from a 1% transfer tax on all real property transactions.

The retail sales tax is regressive but more broad-based than the income tax. Based on 2008 data, sales tax revenues would have to increase by a little more than 7% to match the revenue from a 1% transfer tax.

Effects on the Real Estate Market

As public policy, taxes are more than just generators of revenue. They also affect decisions in private markets that can affect how well the tax raises funds and create incentives and penalties that determine how resources are allocated. In fact, some taxes are intended more to affect decisions than to raise money. An example is the "sin" tax, such as that on tobacco sales. It is desirable for a tax to be as **market-neutral** as possible if its intended purpose is to raise revenues, not to reward or punish a certain behavior.

The RETT has the potential to affect both the demand for and supply of real property. The tax produces a "wedge" that either raises the cost to the buyer without encouraging more supply (if the buyer pays the tax) or lowers the proceeds to the seller without stimulating demand (when the seller pays the tax). If the tax is substantial and transparent (the buyer is apprised of the costs through the lender's required good-faith estimate), it could **reduce the number of sales and lower property values**. Empirical studies exist that document such effects.

A RETT borne by the buyer will **reduce demand**, all other things held constant. The higher costs make substitutes (renting, staying put, or buying in an untaxed jurisdiction) more attractive and price some buyers out of the market. The result of reduced demand is a smaller number of sales. The effect is especially potent because the tax requires a cash contribution at closing, and cash is critical in a transaction. Sellers could pay the expense through seller concessions, then attempt to shift some back to the buyer through a higher sales price. In that way, the buyer could finance some of the expense. This mechanism depends on the property appraising high enough and the buyer being able to qualify for the increased loan.

When the tax is high, the effect on sales can be profound. In one study, a RETT was imposed by a city in addition to the one affecting surrounding jurisdictions. The analyst monitored sales on either side of the city border and used statistical techniques to isolate the effect of the tax differential. The study found that a city RETT varying from 0.4% to 2% of value caused the **number of sales to be 16% lower** within the city border. The differential was even higher for entry-level homes, despite the city's policy of giving a partial refund to first time homebuyers.

A RETT can have an effect on prices, as well. A seller facing reduced demand because of the tax might lower the asking price a bit to induce a sale. This could manifest itself as a **reduction in sales price** or as a seller concession in paying the tax on behalf of the buyer. The effect would be greater when market conditions favor buyers and when buyers are especially sensitive to closing costs (both conditions were characteristic of housing markets in 2010). The maximum amount of price differential expected equals the amount of the tax (a 1% tax should result in no more than a 1% decline). Empirical studies of the effect on home sales prices indicate a slightly larger discount. Researchers attribute this result to buyers anticipating a lower sales price when they inevitably sell the home in the future.

Impact on Housing Affordability

One of the more detrimental effects of a RETT is the **increased difficulty for those hoping to buy a home**. Owning a home is considered a fundamental financial accomplishment. The RETT not only raises the bar for those buying a first home but diminishes the attractiveness of homeownership by making the home harder to re-sell. It would be ironic if a policy designed to provide affordable housing to a few families (Housing Trust Fund) were to result in denying homeownership to an even greater number.

Housing affordability is often monitored by estimating how much income would be needed to buy the average-priced home in a given market and comparing that to the local median income. The relationship can be expressed as the percentage of local households able to afford a median-priced home. It is assumed that all households require financing at market terms and possess the cash down payment necessary to arrange the purchase. The income needed to purchase the home is determined by the lender's qualifying criteria (the so-called "front end" maximum ratio of house payment to monthly income).

Affordability is determined largely by interest rates and housing prices. However, the concept can be used to gain perspective on how an **increase in transaction costs could hamper the ability to buy a home**. If it is assumed that the tax amount can be added to the loan amount, applying the affordability criteria indicates how many fewer households could afford the average home. Table 2 shows how many households would no longer be able to afford the average-priced home if a 1% RETT were imposed (the number of households that would be priced out of the market by the addition of a RETT to the financed amount). The calculation assumes conventional financing with a 20% cash down payment. Shown are the results at the state and local (New Orleans) levels. It should be noted that the households that can no longer afford the average-priced home might still be able to afford a less expensive home. The calculation provides context for how many households would be affected by the tax.

Table 2

Impact of a 1% Transfer Tax on the Ability of Households to Afford the Average-Priced Home

	Louisiana	**New Orleans**
House price*	$183,522	$204,115
Current regime:		
Loan amount	$146,818	$163,292
Monthly payment	$1,093.90	$1,216.66
Income to qualify	$46,881	$52,143
% households that can afford	47.4	34.9
Number that can afford	797,815	151,733
Imposition of 1% tax		
Loan amount	$148,653	$165,333
Monthly payment	$1,103.75	$1,227.61
Income to qualify	$47,304	$52,612
% households that can afford	47.1	34.5
Number that can afford	792,260	150,079
Households that can no longer afford	5,556	1,653

*Based on 2008 annual average prices.

Data sources: Louisiana Association of Realtors, U.S. Census Bureau, Bankrate.com.

Even more telling is the number of non-homeowners, defined as renting households, that would be unable to afford an entry level home. For the calculation, it is assumed that a low–down payment loan (insured by the FHA) is relied upon to buy a typical starter home valued at $100,000. Table 3 shows how many renters would be unable to become homeowners because of a 1% RETT.

Table 3

Impact of a 1% Transfer Tax on the Ability of New Orleans Renters to Afford a $100,000 Home

House price	$100,000
Current regime:	
Loan amount	$96,500
Monthly payment	$739.64
Income to qualify	$30,606
% households that can afford	41.4
Number households that can afford	57,697
Imposition of 1% tax	
Loan amount	$97,500
Monthly payment	$745.58
Income to qualify	$30,851
% households that can afford	41.0
Number households that can afford	57,140
Households that can no longer afford	557

All these estimates rest on a homebuyer's ability to finance the increased costs. In the very likely case that the increased cost would require additional cash, the impact would likely be more extensive. Cash requirements are considered the most significant barrier to becoming a homeowner. The problem will only become more serious as the FHA moves, as it has announced, to increase its upfront premium and to reduce the amount of buyer expense paid by the seller. To lessen the problem, some states exempt first-time homeowners from their RETT.

Conclusion

Like motherhood, apple pie, and the American flag, the goal of achieving affordable housing for all Americans is a highly worthy one.

However, singling out one small sector of the economy to pay the full amount is an inequitable bad idea. Discriminating against this segment, composed mostly of middle-income home buyers and sellers, brings socially undesirable results. It raises the financial hurdles for homebuyers (home buying is an activity to be treasured) and shuts some out of the market. Unlike user fees whereby most of the cost of public facilities is borne by those who benefit (such as a tax on gasoline that is used to improve highways), a RETT is imposed on those who do not specifically benefit from expenditure of the proceeds. In addition, the RETT base is too small and volatile to provide a stable source of funding.

Property taxes have been largely relegated as the prime source of revenues for local governments. Adding to this tax would not be a viable source of additional revenue at the state level. The state of Louisiana does have personal and corporate income taxes, a sales tax, and special taxes on alcoholic beverages, as well as a state lottery. Any of these could be tapped to fund new programs.

Home buyers or sellers ought not be forced to be sole targets of a tax from which they do not specifically benefit. Services that provide general benefits should be funded from broad-based, stable revenue sources.

Glossary

Discretionary income—income that is left over after expenditures for necessities, such as food and shelter, and taxes.

Effective tax rate—the amount of tax paid as a percentage of income or total asset value. The effective tax rate can be used to compare the burden of a tax to that of alternative taxes.

Equity (tax)—fairness, or how taxpayers are treated relative to one another. There are two economic criteria for tax equity: tax burden should be commensurate with benefits derived, and tax burden should be relative to taxpayer's ability to pay the tax.

Housing affordability—comparison of the expense of buying a home to the buyer's income. Often measured by the ratio of median income of an area's residents to the income needed to buy the median-priced home in the area. Can also be expressed as the percentage of households in an area that can afford to buy the median-priced home. Ability to purchase is related to the ability to qualify for financing sufficient to buy the home with a standard down payment.

Impact fees—special assessments levied on housing developments for the purpose of offsetting the costs of extending public services to serve the new subdivisions.

Louisiana Housing Trust Fund—a program administered by the Louisiana Housing Finance Agency that develops owner-occupied and rental housing for lower-income residents.

NAR—National Association of Realtors, an organization of real estate agents that provides educational, professional and legislative services to its members. State and local affiliates maintain multiple listing services that facilitate the marketing of residential properties.

Progressive (tax)—tax rate increases as income increases. Progressivity is achieved by increasing the rate of tax with income, such as the graduated tax rates applied to taxable income by the federal income tax.

Proportional (tax)—tax burden is uniform compared to income. A flat rate applied to income, broadly defined, would be an example of a proportional tax. The tax burden is the same for all income groups.

Regressive (tax)—tax burden decreases as income decreases. The amount of tax paid represents a greater percentage of income as income declines. A regressive tax may impose a uniform tax rate but be applied to an asset that is increasingly important component to those of low income or wealth.

RETT—real estate transfer tax. Also called a land transfer tax or a real estate excise tax. A tax that is assessed when a real property changes ownership, often in conjunction with the deed being recorded into the public record. RETTs are distinguished from recording fees by their much higher levy as a percentage of the value of the property transferred.

Appendix

Tax Rates by State

Table A-1

State Real Estate Transfer/Deed Recordation Taxes

State	Description	Rate	2004 State Revenue ($000)	2004 State Revenue Per Capita
Alabama	$.50 per $500 of property conveyed	0.10%	$45,080	$9.95
Arizona	$2 per deed required to be recorded	NA	NA	NA
Arkansas	$3.30 per $1,000 of consideration in excess of $100	0.33%	$25,972	$9.43
California	Local taxes only		NA	NA
Colorado	$.01 per $100 of consideration in excess of $500	0.01%	NA	NA
Connecticut	1.25 percent of consideration paid if consideration exceeds $2,000 -- Other rates for commercial transfers	1.25%	$175,816	$50.18
District of Columbia	2.2 percent of consideration or fair market value	2.20%	$286,269	$485.20
Delaware	2-3 percent (depending on local tax) on transfers in excess of $100; 1 percent on contracts for improvements to realty in excess of $10,000	2.0–3.0%	$98,566	$118.74
Florida	$.70 per $100 of consideration except in Miami-Dade County where it is $.60 per $100	0.70%	$1,950,402	$111.99*
Georgia	$1 for first $1,000 of consideration plus $.10 per $100 of additional consideration	0.10%	$420	$0.05
Hawaii	$.10 per $100 of consideration	0.10%	$18,426	$14.59
Illinois	$.50 per each $500 of value or fraction of $50	0.10%	NA	NA
Iowa	$.80 per $500 paid for the real property transferred	0.16%	$13,869	$4.69
Kansas	0.26 percent of debt or obligation secured by real estate	0.26%	$52,569	$14.59
Kentucky	$.50 per $500 of value conveyed in deed	0.10%	$3,434	$0.83
Louisiana	Local taxes only			
Maine	$2.20 per $500 of value conveyed - Split between grantor and grantee	0.44%	$29,380	$22.31
Maryland	0.5 percent of consideration paid for realty -- Also local deed recordation taxes ranging from $2.20-$5.00 per $500 of value and local transfer taxes ranging up to 1.5 percent of consideration paid	Variable depending on local rates	$183,189	$32.96
Massachusetts	$4.56 per $1,000 of consideration	0.456%	$245,906	$38.32

State	Description	Rate	2004 State Revenue ($000)	2004 State Revenue Per Capita
Michigan	$3.75 per $500 of value for property being transferred plus local taxes of $.55 - $.75 per $500 of value	0.75%	$317,480	$31.39
Minnesota	$1.65 plus .33 percent of value in excess of $500 plus .23 percent of debt secured by real estate for mortgage registry	0.56%	$352,354	$69.08
Nebraska	$2.25 per $1,000 of value transferred	0.225%	$9,215	$5.27
Nevada	$1.95 - $2.55 per $500 of consideration depending on population of county	0.255% max.	$96,704	$41.41
New Hampshire	$1.50 per $100 of consideration split equally between buyer and seller	1.50%	$145,386	$111.82
New Jersey	Four transfer fees -- Basic is $1.25 state and $.50 county each $500 of consideration; additional fees range from $.25 - $4.30 per $500 of consideration; a fifth fee of 1 percent is imposed on buyers for an entire consideration in excess of $1 million for certain residential and farmland property	1.21% max. if less than $1 million	$246,503	$28.34
New York	$2.00 per $500 of consideration. An additional 1 percent on transfers of a personal residence of more than $1 million	0.4% on the basic tax plus and additional 1.0% on residence over $1 million	$510,443	$26.55
North Carolina	$1 per $500 of consideration or value transferred with 51 percent of revenue retained at local level	0.20%	$54,940	$6.43
Ohio	Local taxes only ranging from $.10 -$.40 per $100 of value	0.4% max.		
Oklahoma	$.75 per $500 of consideration	0.15%	$12,048	$3.42
Pennsylvania	1 percent of consideration or fair market value with local transfer taxes of 1 - 3 percent	4.0% max.	$470,789	$37.95
Rhode Island	$2 per $500 of consideration	0.40%	$12,645	$11.70
South Carolina	$1.85 per $500 of value with $.55 per $500 retained at the local level	0.37%	$50,493	$12.03
South Dakota	$.50 per $500 of consideration payable by grantor	0.10%	$141	$0.18
Tennessee	$.37 per $100 of consideration plus a mortgage tax of $.115 per $100 of indebtedness in excess of $2,000	0.485%	$174,206	$29.52
Vermont	1.25 percent of value of property transferred; lower rates on certain homes and farms	1.25% max.	$20,762	$33.43
Virginia	$.25 per $100 of conveyance plus $.50 per $500 of consideration for transfer of realty	0.35%	$340,591	$45.66

State	Description	Rate	2004 State Revenue ($000)	2004 State Revenue Per Capita
Washington	1.28 percent of selling price plus local tax of 0.3-0.5 percent	1.33$% max.	$640,086	$103.17
West Virginia	$1.10 per $500 of consideration plus local taxes that may run to another $1.10 per $500	0.44% max.	$10,129	$5.58
Wisconsin	$.30 per $100 of value	0.30%	$66,325	$12.04
U.S. Total			$6,615,458	25.33†

*Revenue figures adjusted to eliminate taxes other than real estate transfers in the Census Bureau figures.

†U.S. median

Source: Compilation by the Federation of Tax Administrators (FTA), based on CCH, *State Tax Handbook* (2006), data from the U.S. Bureau of the Census, Governments Division, and information from individual states; posted at http://www.taxadmin.org/fta/rate/Realtytransfer.html.

Calculation Of Effective Tax Rates

The *American Housing Survey* is published jointly by the U.S. Census Bureau and the Department of Housing and Urban Development. The national report comes out every other year, and a similar report is published on a selected group of metropolitan areas approximately every fifth year. The AHS concentrates on housing and provides items of data not found in the ten-year population census. Among those items is median value of homes owned, as reported by household income. These data permit estimates of effective tax rate based on a proposed RETT. Another item of data indicates how many homeowners have moved during the previous year. The reciprocal of the percentage of movers gives an indication of average tenure—the period between moves. This estimate is used to calculate total income earned between moves, and before another RETT assessment is assessed.

Background data for the calculations are shown in the following tables. The first is based on national data and the second on the New Orleans metropolitan area (unfortunately, the data are not reported by state). The national calculations are intended to show the general regressive nature of the tax and the metro calculations provide a local perspective.

Table A-2

National Homeowners 2007

Income ($)	Median Home Value ($)	Median Annual Income ($)*	Est. Tenure (years)	Median Tenure Income ($)
1–19,999	99,827	11,845	19.9	235,716
20,000–39,999	131,890	28,868	15.2	438,794
40,000–59,999	160,853	50,000	12.1	605,000
60,000–79,999	194,763	70,000	12.4	868,000
80,000–99,999	233,534	90,000	13.3	1,197,000
100,000 and up	356,104	141,468	12.9	1,824,937

*Assumes incomes distributed evenly within brackets.

Table A-3

New Orleans Homeowners 2004

Income ($)	Median Home Value ($)	Median Annual Income ($)*	Est. Tenure (yrs)	Median Tenure Income ($)
1–19,999	86,311	14,091	19.3	271,956
20,000–39,999	97,283	30,315	11.3	312,245
40,000–59,999	125,187	50,000	10.3	515,000
60,000–79,999	130,386	70,000	32.4	2,268,000
80,000–99,999	144,545	90,000	11.7	1,053,000
100,000 and up	224,051	134,366	11.0	1,478,026

*Assumes incomes distributed evenly within brackets.

Calculation of Tax Revenues Needed to Match RETT Proceeds

A RETT usually applies to all real property sales unless specific classes, like first-time homeowner purchases, are exempted. Data on home sales are reported by both the Louisiana Association of Realtors and the National Association of Realtors. The NAR number for the state represents total sales, not merely those closed through the Realtor-operated multiple listing services. However, NAR reports number of sales only (59,100 for 2008). LAR reports average sales price ($183,500 for 2008). Therefore, total sales volume can be estimated by multiplying the NAR total by the average sales price ($10.8 billion). A 1% RETT would yield $108 million. Data on the volume of commercial sales is not available. As a generous estimate, it is assumed that non-housing sales yield another $108 million in tax revenue, for a total of $216 million.

Collections from existing taxes are reported in the Louisiana Department of Revenue's annual report, *Annual Tax Collection Report.* For fiscal year 2008, reported proceeds were $2,883 million for the sales tax and $3,242 million for the individual income tax. A 7% increase in either of these taxes would yield slightly more than $200 million, based on 2008 conditions.

Calculation of Affordability Effects

The National Association of Realtors calculates its Housing Affordability Index as the ratio of median family income to the income required to buy a median-priced home, based on current sales prices and mortgage loan terms. The required income number is based on lenders' qualifying criteria for conventional loans with a 20% cash down payment. The Fannie Mae/Freddie Mac standard maximum monthly payment-to-income ratio is 28%, with the monthly payment defined as principal repayment, interest, property taxes, and hazard insurance premium (PITI). For the calculations used in this report, current mortgage interest rates were taken as those reported by Bankrate.com for conventional, fixed rate loans with a 30-year term. Tax and insurance escrow payments were estimated at 2% of property value per year. The impact of the RETT was estimated by adding the tax burden to the mortgage loan and estimating the difference made to qualifying income. Average home sales price was calculated from sales data reported by the Louisiana Association of Realtors in its monthly *Trend* publication.

Instead of comparing the qualifying income to the median income, as the Housing Affordability Index does, this analysis estimates the percentage and number of households earning at least that amount of income. The estimate requires the distribution of households by income for the state and metro area. The Louisiana distribution is available from the 2000 Census of Population; the New Orleans data are taken from the 2004 American Housing Survey. To project these data so as to make them comparable to 2008 house prices, the boundaries of the income brackets were inflated by the rate of growth for median household income for the period of the projection. Thus, the state distribution was inflated by the median growth from 2000 to 2008 and the metro by the rate from 2004 to 2008. This technique rests on the assumption that the shape of the distribution was unchanged over the projection period. After projecting the numbers, a cumulative income distribution was produced (see charts). With this distribution, it is possible to estimate the percentage of households with income below any given amount.

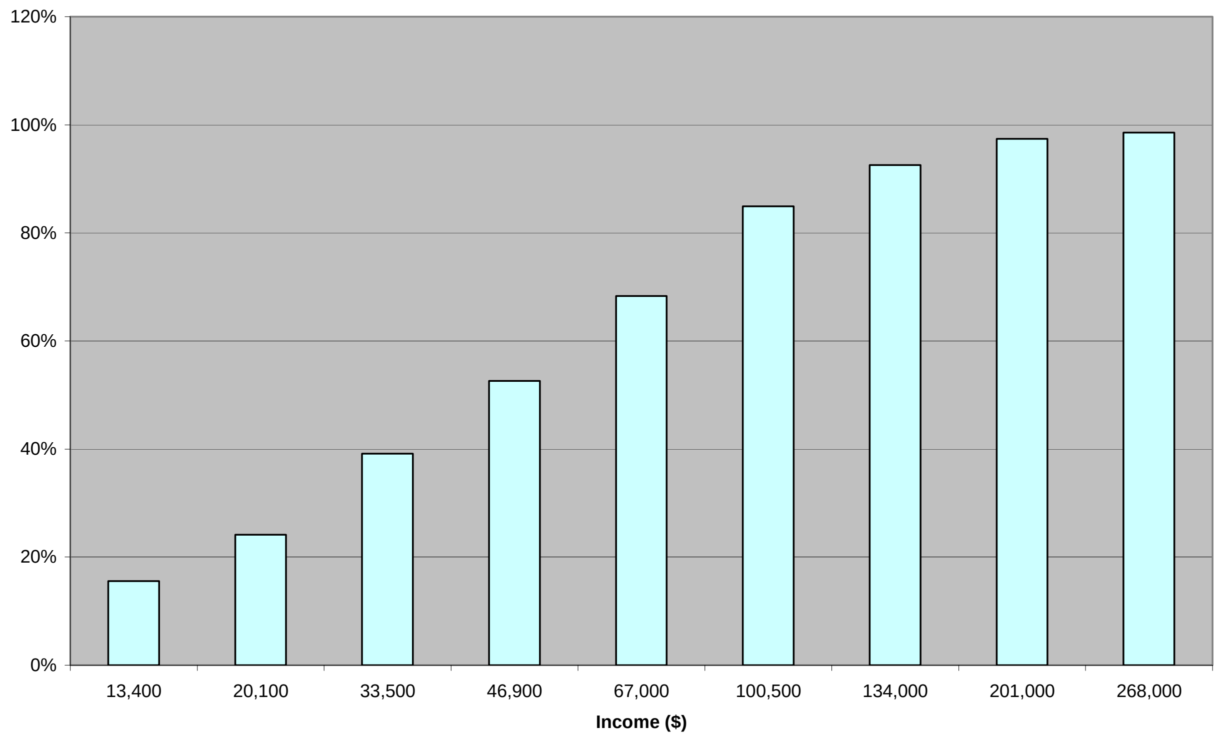
Affordability is a serious problem for first-time homebuyers. High interest rates and/or high house prices can effectively shut non-owners out of the market and disrupt the flow of new homeowners. To demonstrate the effect of a RETT on entry-level affordability, an analysis focuses on how many renter households would no longer be able to afford an entry-level home because of the tax. For this analysis, financing terms are based on the popular FHA 203(b) insurance program. The qualifying ratio and the interest rate are slightly higher for FHA-insured loans. A monthly insurance premium is required as well, and that is included in the monthly payment. The basic analysis is identical to that described above. Income distribution is for renter households (it is assumed homeowners are former renters, rather than newly formed households), which is available from the AHS but not the Census of Population. Therefore, the analysis is possible only for the New Orleans metro area.

Table A-4

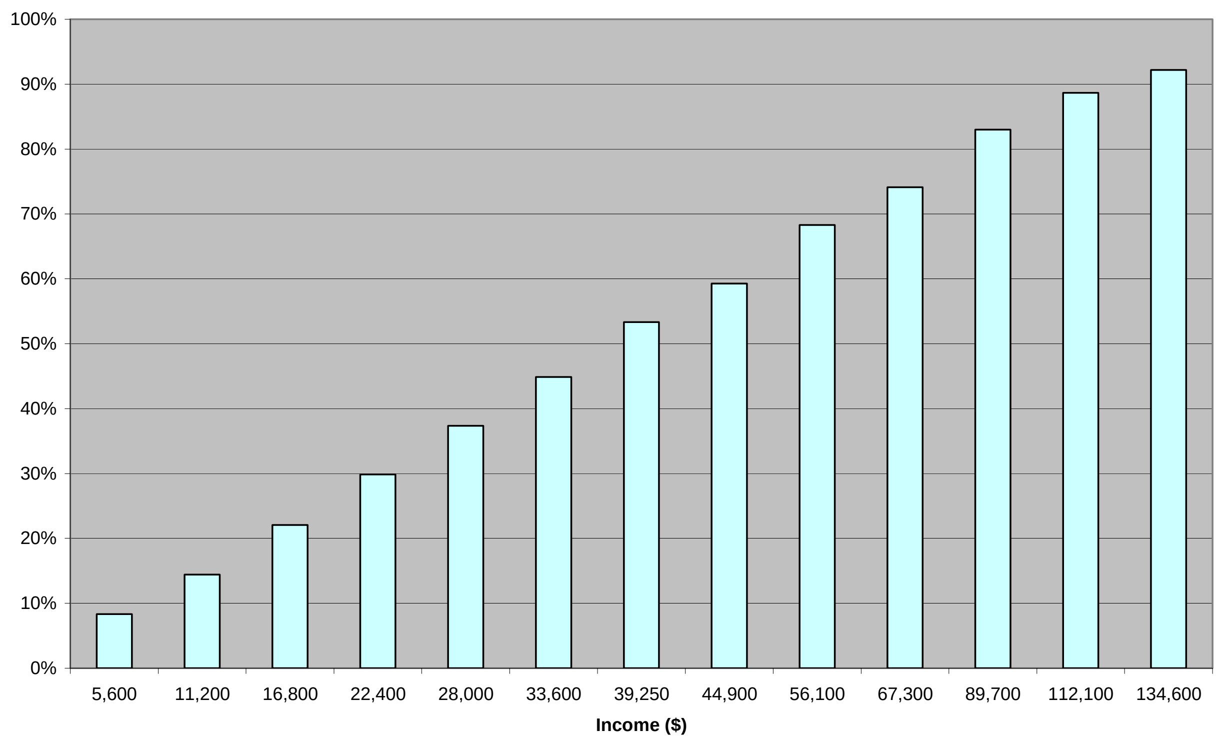
Background Data for Affordability Analysis

	Louisiana All Households	New Orleans All Households	New Orleans Renters
Home price ($)	$183,522	$204,115	$100,000
Loan-to-value ratio	80%	80%	96.5%
Interest rate	5%	5%	5.25%
No RETT			
Loan principal	$146,818	$163,292	$96,500
Loan payment	$788.03	$876.47	$532.76
Escrow	$305.87	$340.19	$166.67
MIP	$0	$0	$40.21
PITI)	$1,093.90	$1,216.66	$739.64
Qualifying income	$46,881	$52,143	$30,606
Qualifying households (%)	47.4%	34.9%	41.4%
Qualifying households (no.)	797,815	151,733	57,697
RETT .5% value			
Loan principal	147,735	164,313	97,000
Loan payment	792.95	881.95	535.52
Escrow	305.87	340.19	166.67
MIP	0	0	40.42
PITI	1,098.82	1,222.14	742.61
Qualifying income	47,092	52,377	30,729
Qualifying households (%)	47.2	34.7	41.2
Qualifying households (no.)	795,122	150,863	57,419
Households lost	2,694	870	279
RETT 1% value			
Loan principal	148,653	165,333	97,500
Loan payment	797.88	887.42	538.28
Escrow	305.87	340.19	166.67
MIP	0	0	40.63
PITI	1,103.75	1,227.61	745.58
Qualifying income	47,304	52,612	30,851
Qualifying households (%)	47.1	34.5	41.0
Qualifying households (no.)	792,260	150,079	57,140
Households lost	5,556	1,653	557

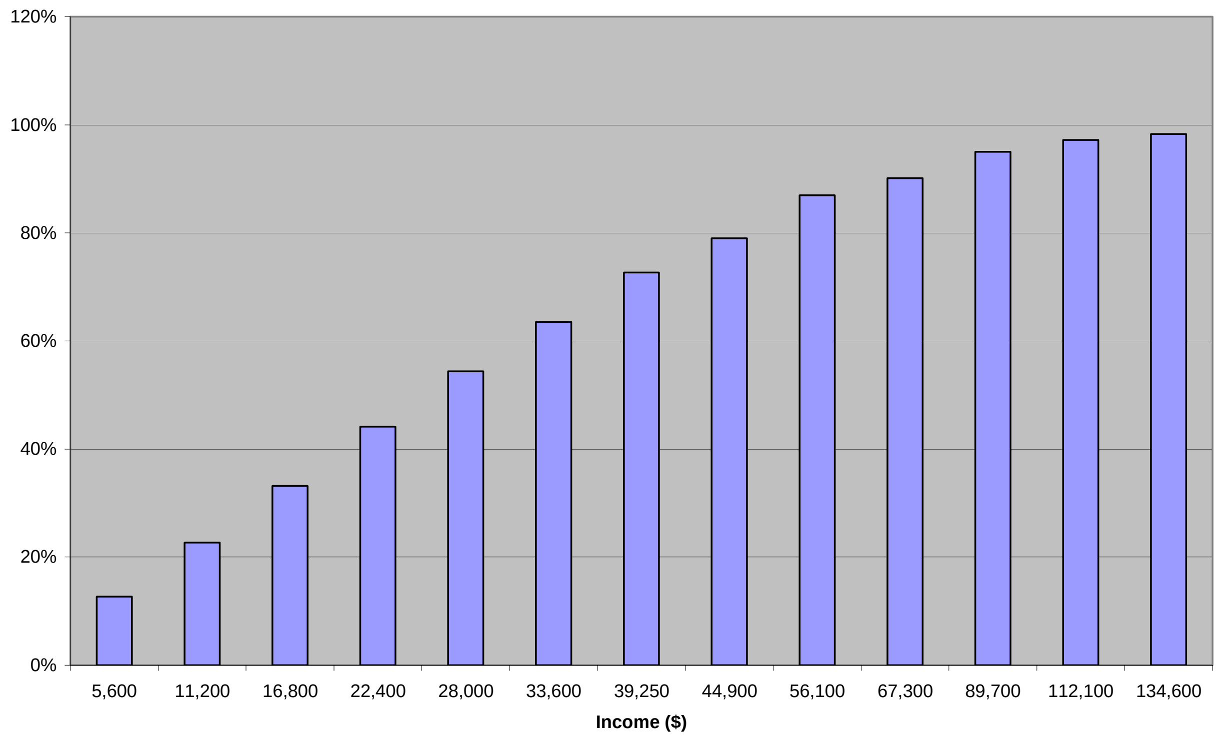
Percentage of Louisiana Households Earning Less Than Specified Annual Income



New Orleans Households Earning Less Than Specified Annual Income



New Orleans Renter Households Earning Less Than Specified Annual Income



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