

# The Costs and Challenges of Tax Swaps

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# Four Types of Tax Swaps

State for State

State for Local

Local for State

Local for Local

# Tax Swap Challenges

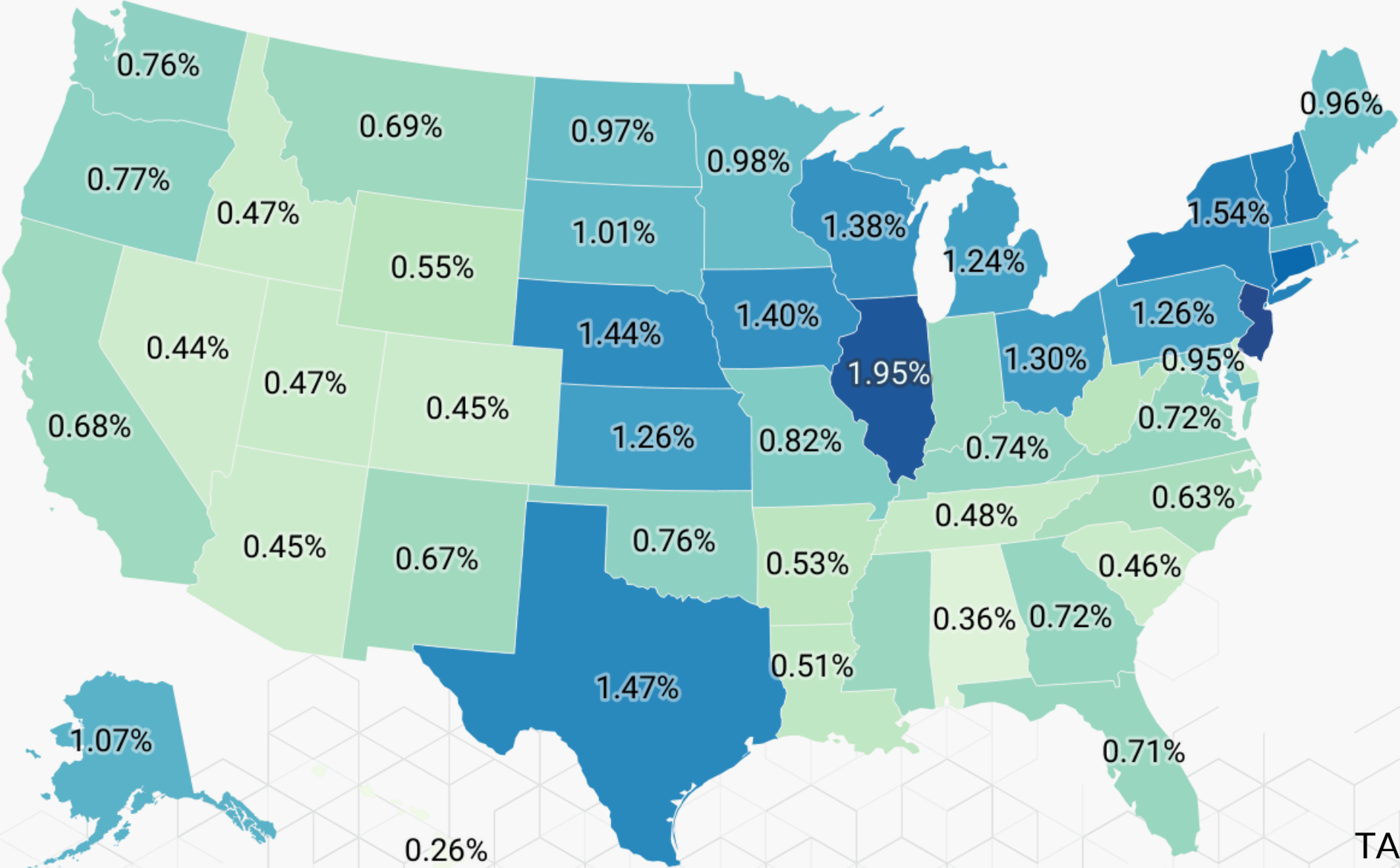
Achieving Distributional Fairness

Calculating Future Distributions

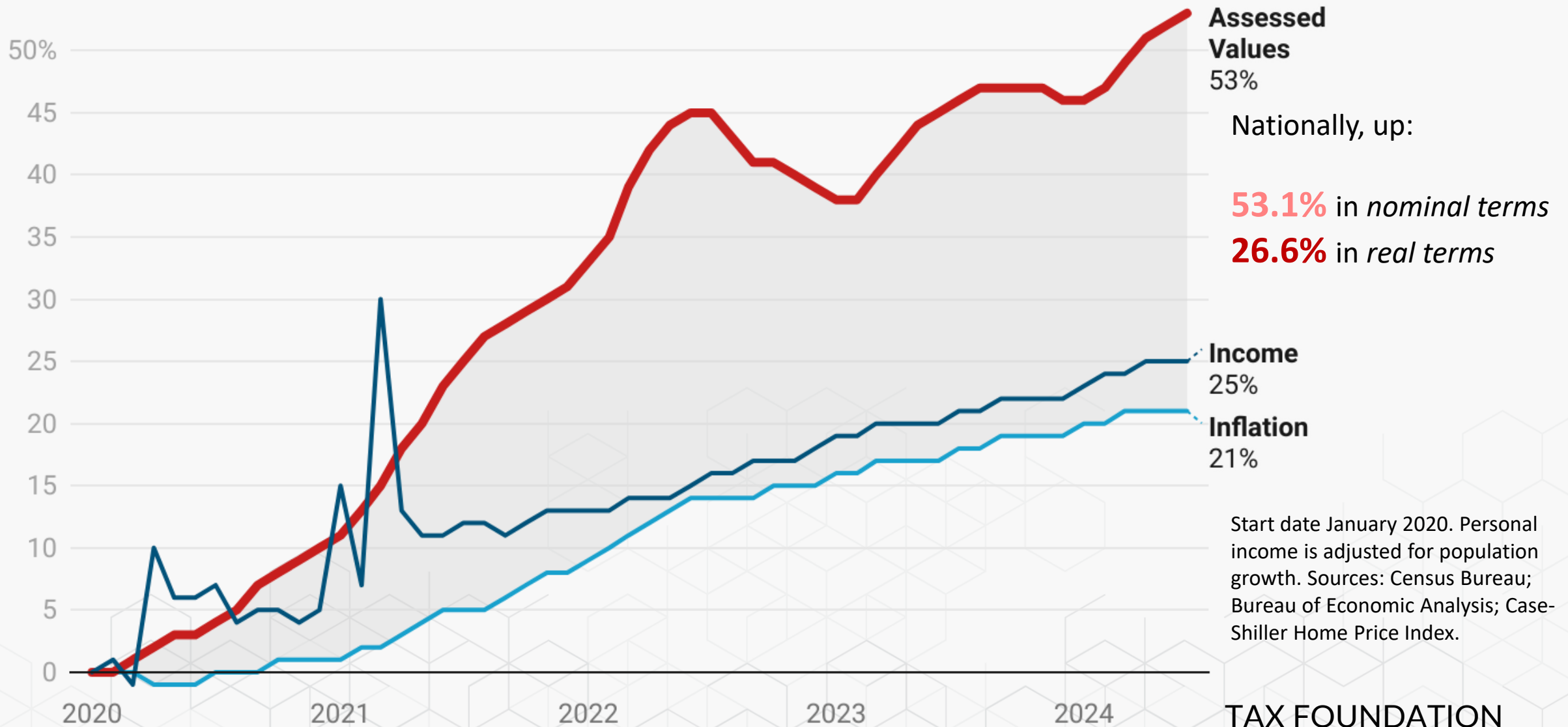
Safeguarding Against Overall Tax Hikes

Avoiding a Shift to Less Competitive Taxes

# Homeowners' Effective Rates



# Assessed Values Rising Faster than Inflation



# The Case for Property Taxes

1. Property taxes **do less economic harm** than alternative ways to raise the same amount of revenue, making them more economically efficient than the alternatives.
2. Property taxes **have less of an effect on decision-making**—including location decisions—than most other taxes, making them less distortionary than the alternatives.
3. Property taxes **roughly align with the benefits** that property owners receive from local services, making them more equitable than the alternatives.
4. Property taxes are **highly transparent** and correlate strongly with services that enhance the value and utility of property, making them unusually sensitive to local preferences on size and scope of government.

# Economic Efficiency of Property Taxation

- A 1 percentage point shift from income taxes to sales taxes improves GDP by 0.74%, while shifting to property taxes **increases GDP by 1.45%**  
~ Arnold, Brys, Heady, Johansson, Schweltnus, & Vartia, *Economic Journal*
- A 1 percentage point shift from income to consumption taxes increased GDP by 0.92%, while a shift to property taxes yielded a **1.22% GDP improvement**  
~ International Monetary Fund
- Gross state product **decreases by 2.8%** when the income tax replaces the property tax, while household income **declines by 3.47%**  
~ Faulk, Thairprasert, & Hicks, Ball State working paper
- While a 1 percentage point higher rate on *personal* property reduces annual employment growth by 2.44%, higher *real* property taxes actually correspond to **modestly increased rates of employment growth**, likely because the business benefits of higher local spending are greater than the additional tax costs  
~ Mark, McGuire, & Papke, *National Tax Journal*

# Why are Property Taxes More Efficient?

- Land is a fixed asset
  - The supply of land itself does not change with property taxes, and elasticities on supply of housing are favorable
- Does relatively little to distort economic decision-making
  - Even taxing improvements isn't as harmful as it might be, since the tax on the value of unimproved land encourages efficient land use
- Does not penalize productivity or consumption
  - Contrasts with income and sales taxes, which reduce incentives to work, invest, or consume
- Tax is capitalized into home prices
  - Can't avoid impact of increase by moving





# Questions?

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