Over-Assessment of Affordable Housing Impacts Homeowners

By Jack F. Stucker, Judy F. Berkman and Mark S. Schwartz

In February, the city of Philadelphia started notifying homeowners of their 2014 property values under the Actual Value Initiative. There has been ample media coverage that the values increased dramatically in some neighborhoods, while other values stayed the same or went down. This spring, Philadelphia City Council will consider the ordinances that will set the new tax rate, taking into account a proposed $15,000 homestead exemption and other potential programs for vulnerable owner occupants, including long-time owners in gentrifying neighborhoods.

A decade ago, public funds were flowing to help develop low-income and workforce homeownership housing. Even now, various government-funded down payment and closing cost assistance programs are still available. No matter what the subsidy, each program has strings attached in the form of "soft" mortgages and/or deed restrictions. The programs can be layered so that one buyer may have a conventional first mortgage and up to four additional "soft" mortgages to secure the funders' investments and to prevent the buyer from "flipping" the house and being unjustly enriched.

These affordability restrictions generally require the buyer to occupy the home as the buyer's principal residence, but the buyers are also often prohibited from leasing and any other income-producing uses. Invariably the restrictions include various resale restrictions to keep the home affordable for a term of years. The owners may not know these restrictions affect the valuation of their homes for real estate tax purposes.

These affordability restrictions also mean that owners who may not be able to afford a tax increase at full market value cannot take the steps someone in an unrestricted home might do. Or, if an owner decides to sell the home during the affordability period, the "soft" mortgages kick in to "recapture" the principal, limit the sale price, or impose income eligibility criteria for the next buyer. While some of these restrictions could be easily identified for a 50-unit development, other restrictions may be more challenging to identify, since a program may exist for a short time, be targeted to a geographic area or population, and or be provided by a pass-through source like a bank.

Such an unfair over-assessment of a subsidized home may make it difficult for a homeowner to handle the increased mortgage payments on a tight monthly budget. Or, the problem may pop up when the owner's 10-year tax abatement on the improvements expires, and the owner must start paying much higher real estate taxes, although the affordability restrictions could remain in effect another five years.

In 2003, affordable housing developers, lenders and investors had pointed out that low-income housing developments were being taxed using a market comparison method that was unfair and threatened their economic viability. Local assessors were using a market comparison method to determine actual value of property, including property subject to affordability restrictions. However, as in *Parkside Townhomes Associates v. Board of Assessment Appeals of York County*, 711 A.2d 607, 609 (Pa. Comm. 1997), this market comparison method did not take into consideration such restrictions.

As a result of this advocacy, Pennsylvania enacted a law in 2003, 72 P.S. §5020-402(c)(1), governing real estate assessments of affordable housing that provided: "In arriving at the actual value of real property, the impact of applicable rent restrictions, affordability requirements or any other related restrictions prescribed by any federal or state programs shall be considered."

The 2003 law clarified, but did little to change, Pennsylvania assessment law, which requires that properties be assessed at their actual value. It is well-established in *Vollmer v. Philadelphia*, 38 A.2d 266, 269 (Pa. 1944), that "this means nothing more or less than market value. [The Pennsylvania Supreme Court has] defined market value as the price which a purchaser willing but not obliged to buy, would pay an owner, willing but not obliged to sell, taking into consideration all uses to which the property is adapted and might in reason be applied."

The valuation considerations required by the 2003 law were affirmed as applied in the 2008 case, *1198 Butler St. Associates v. Board of Assessment Appeals, County of Northampton*, 946 A.2d 1131,1133 (Pa. Comm. 2008). In *1198 Butler*, the court took note that the 2003 law is consistent with prior case law addressing the effect of rent restrictions. The *1198 Butler* court affirmed the trial court's finding that "to ignore [the restrictions imposed by covenants required to qualify for the Federal Low-Income Housing Tax Credit program] is a failure that effectively provides a distorted valuation for tax purposes relating to [the properties at issue]."

How has this law been applied over the past decade? Taxing authorities throughout Pennsylvania now apply the 2003 law reasonably well to affordable housing rental projects, which has ensured the continued viability of these important developments in Pennsylvania.

Missing from the public discussion, and likely unbeknownst to affected owners in Pennsylvania, is how real estate tax assessors apply the 2003 law to homeownership properties with affordability restrictions. Even if the assessors consider some restrictions, there is not a transparent process to take all the restrictions into account. This raises the question whether assessors are unwittingly imposing unfair property tax burdens on properties with affordability restrictions. This should be of concern not only to homeowners, but also their lenders, and the public entities that funded the transactions and imposed the restrictions.

Unfortunately, for individual low-income homeowners whose homes are subject to affordability restrictions, there are barriers to challenging an unfair assessment. A homeowner who is aware of the issue and who believes the local taxing authority has failed to properly consider the 2003 law is burdened by the presumptive validity of the assessment. Unless the owner submitted a timely request for an informal review, which is a new option in Philadelphia, the aggrieved homeowner must present sufficient competent, credible and relevant evidence to succeed in overcoming the presumed validity of the tax.

Bearing the cost to dispute an assessment may be an economically sound decision for the owner of an affordable rental development. However, a low-income homeowner's real estate tax differential is likely not worth the cost to hire legal counsel and an appraiser to appeal an assessment. Moreover, it would be unfair to require each and every homeowner subject to similar affordability restrictions to appeal, especially where the affordability restrictions were imposed by the taxing jurisdictions.

Enactment of the 2003 law has ensured that Pennsylvania continues to benefit from new investment utilizing subsidized rental housing development programs. Likewise, assessors also need to consider any affordability restrictions on low-income homeowners' properties. The impact could mean the difference between sustainable homeownership and foreclosure. •

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