

# Parcel Taxes With Perfectly Attentive Homeowners

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If you vote in California, then you have probably seen a parcel tax proposal on your ballot. There are thousands of cities, counties, and other local government districts that can add (voter-approved) parcel taxes to the property tax bills of the city, county, or district's residents to fund local government services. This system creates not only an abundance of districts offering various levels and types of local government services, but also a method for adding to this abundance. What are the implications of such a system with an imperfectly attentive populous that sometimes pays too much and sometimes too little attention to parcel taxes?

First, consider the hundreds of existing parcel taxes and their associated districts. In theory, having all of these options is good for perfectly attentive consumers. When consumers have choice, they can vote with their feet by choosing to live in a location that has the local government services that suit them best. In practice, consumers, in this case home buyers, are not perfectly attentive. Some theory and evidence suggest that buyers pay too little attention to these sorts of parcel taxes. One reason is that there is a multitude of relevant features to consider when buying a home, so parcel taxes might not be particularly salient to the buyer, that is, these taxes do not grab the buyer's attention. As a result, the buyer ignores the parcel tax. Another reason buyers may ignore parcel taxes is that a parcel tax feels inconsequential compared to the cost of buying a home: a buyer considering paying \$400,000 for a home may not care if the annual property tax bill is \$4000 or \$4100 (for a \$100 parcel tax). If buyers are not paying attention to the fact that they have choice over local government services, the argument that the parcel tax system benefits consumers by allowing them to choose a location that best suits them falls apart. Though home buyers may not, in practice, benefit from

the abundance of choice, local governments and existing homeowners might. Inattentive buyers will not change their behavior in the presence of taxes, neither avoiding districts with parcel taxes, nor demanding lower prices to compensate for higher tax bills. Both of these outcomes elevate demand and thus home prices, which benefits existing residents and local governments (because higher home prices translate to more property tax revenue).

Just as the implications of existing parcel taxes differ in theory and in practice, so too is the case with the ability to add new parcel taxes to an existing area. In theory, existing residents benefit from the ability to propose new parcel taxes. The result, a better match between the government services a resident wants and those that are offered, is similar to the benefit home buyers get from the ability to choose between districts; rather than finding a good fit, residents create one. Not all residents benefit from the ability to add new parcel taxes. Those who vote against a parcel tax proposal that ultimately passes may be made worse off because moving is costly. If moving were not costly, these residents would be able to vote with their feet and leave the district with the newly passed parcel tax. Because moving is costly, they are stuck paying for something they do not value. In practice, imperfectly attentive consumers could temper both of these theoretical implications. The type of imperfect attention here is not too little attention, but too much. Facing a vote on a parcel tax (say of \$100 per year) focuses voters' attention, making that tax acutely salient. In addition, the way these proposals are framed encourages voters to think about the decision as a choice between paying \$0 (voting no) and \$100 (voting yes) more per year in property tax, rather than as a choice between paying \$3000 and \$3100 per year. The \$0 vs \$100 framing heightens voters' sensitivity (and aversion) to

the costs of the tax, increasing the likelihood that voters will vote against the parcel tax. As a result, there may be fewer parcel taxes than there would be in a world with perfect attention, which hinders current residents' ability to align the level of government services with their desired level of services. Moreover, because existing residents control the approval of new parcel taxes, excess sensitivity that encourages "no" votes effectively constricts the choices that are available to potential future residents, which harms these future residents. There is a silver lining to a reduction in the number of parcel taxes that are passed: residents who would still vote against a parcel tax in a world of perfect attention do not have to pay for services that they do not value.

Distilling the discussion above, the implications of California's parcel tax system with imperfectly attentive consumers are mixed. Existing residents' over sensitivity to parcel taxes may limit the number of options available both for themselves and for future residents, but future residents may not even be paying attention to the fact that they have choice. In addition, buyers' inattention may keep home prices higher than they otherwise would be, which is ultimately good for current residents and local governments. While there are other implications of the existing parcel tax system (on equity, efficiency, and mobility, to name a few), imperfect attention does not, on net, unambiguously seem to be a problem in need of a solution.