"Proposition 13: An Equilibrium Analysis" (joint with Kyle Matobe and Selale Tuzel)

In 1978, California passed Proposition 13, which stipulated rolling back property assessments for tax purposes to 1975 market value levels, and restricted future property tax increases. This was one of the most significant tax changes initiated by voters in the United States, and since then fifteen other states have passed similar measures. Despite the popularity of Proposition 13 among the voters, it remains to be controversial, partly due to its revenue implications, and discussions about its impact and possible modifications to it continue.

In this paper, we examine the consequences of Proposition 13 and evaluate the results of possible changes to the law in an economy populated with overlapping generations of agents who derive utility from consumption of goods and housing. We study the steady state implications of Proposition 13 on house prices, housing choices, turnover over the life cycle, and welfare of the households. We find that Proposition 13 distorts housing choices by lowering turnover and smoothing housing consumption over the life cycle. Despite the lower tax burden imposed by this regime, the impact of Proposition 13 on house prices is relatively small.

We also study the transition dynamics of moving from an economy featuring Proposition 13 to alternative revenue-neutral regimes with proportional real estate taxes. Without transaction costs, elimination of Proposition 13 leads to immediate reallocation of housing across generations with a significant impact on house prices. However, transactions costs slow down adjustments in housing, reducing the quantitative impact of removing Proposition 13. We find that younger households typically favor alternative regimes, whereas most middle-aged and older households prefer the status-quo with Proposition 13.