The Real Estate Transfer Tax: An Alternative Source Of Park Acquisition and Development Funds

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ABSTRACT: A real estate transfer tax is a tax imposed on transfers of real property within a taxing authority’s jurisdiction. It has been used by a number of jurisdictions as a source of funding for park acquisitions and development. The rationale for using the transfer tax for this purpose is that the person who buys a home or other property has hastened the decline in available open-space land. The paper gives a brief overview of the history of the real estate transfer tax, describes how it has been implemented in selected state and local jurisdictions, and assesses its strengths and limitations.

KEYWORDS: Real estate transfer tax, park acquisition and development.

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Decreases in federal funding and increases in demand for recreation opportunities have forced many public recreation and park providers at the state and local levels to seek alternative sources of funding. This paper explores the possibilities of expanding the use of the real estate transfer tax as a source of acquisition and development funds. A number of U.S. jurisdictions at both the state and local levels have adopted such a tax and found the funds generated to be a relatively reliable source of capital money for park and recreation agencies.

A real estate transfer tax, sometimes called a documentary stamp tax, is a tax imposed on transfers of real property within a taxing authority’s jurisdiction. It is levied whenever property is sold, granted, assigned, transferred, or otherwise conveyed from one person to another. Maryland and Florida provide the most visible examples of its use in the parks and recreation field. The philosophical justification for using a real estate transfer tax for park acquisition and development was well stated by the commission that initially recommended its implementation in Maryland in 1968. According to the commission,

The idea behind the transfer tax is that the person who buys a home or other property for private use has hastened the decline in available open-space land. By paying a tax at the rate of one half of one percent of the property purchase price, that same person would help to support the buying of land which could be used and enjoyed by the general public. (Maryland DNR 1979)
The principle also relates to mandatory dedication and impact fees. But while they are confined to local urban jurisdictions, the real estate transfer tax can also be used at the state level.

The real estate transfer tax has a long history in the United States, and it has been widely adopted by other countries: in the United Kingdom, for example, it is levied by the central government at the rate of one percent on all houses costing more than $45,000. In the United States, it was first introduced at the federal level in the 1921 Federal Revenue Act, but it was repealed soon thereafter. The Federal Revenue Act of 1932 reinstated it and retained it in effect with periodic amendments until it was repealed in 1965. This Act required that on each deed, instrument, or writing by which any lands, tenements or other realty sold shall be granted, assigned, transferred, or otherwise conveyed to, or vested in, the purchaser or purchasers, or any other person or persons, by his or their direction, when the consideration of value of the interest or property conveyed (exclusive of the value of any lien or encumbrance remaining thereon at the time of sale) exceeds $100, a tax [be levied] at the rate of 55 cents for each $500 or fractional part thereof (U.S. Code 1964).

The main argument supporting repeal of this tax at the federal level was that real estate taxes should be the exclusive prerogative of local and state governments, not the federal government. When the federal tax was repealed, its revenue potential was recognized by several state and local governments, which subsequently adopted it.

In recent years, debate has occurred over whether the real estate transfer tax is an excise tax or a property tax. The distinction is important, since it may determine whether or not municipalities in some states have the constitutional authority to impose it under their powers as home rule cities or according to the specific terms of their particular municipal charters. The complex legal arguments involved in this issue are summarized by Bauer (1981).

The real estate transfer tax is currently being used at the state level for park acquisitions in Maryland and Florida, as well as in a number of municipalities. The characteristics of these programs are discussed in the following sections.

The State of Maryland

In 1968, the State of Maryland was experiencing a substantial increase in population and a resulting shortage in the amount of recreation area necessary for this new population. Observations showed that the number of people being turned away at many state parks sometimes equaled the number that could be accommodated (Maryland DNR 1979).

In the 1968 state legislature, a legislative commission was appointed to consider creating a program to expedite the purchase and development of outdoor recreation lands. The resolution sponsoring the commission’s appointment declared that “valuable recreation areas are rapidly being converted to other uses and lost forever as recreation spaces.” It also observed that land values “are increasing at an alarming rate of 10 percent annually.”
The commission recommended that the state adopt Program Open Space, a "crash program" of land acquisition over a five-year period to erase an estimated deficit on open-space lands of about 50,000 acres. To pay for these improvements, they proposed a $150 million program: $107 million would be financed by the sale of general obligation bonds, and the remainder would come from state revenues from a transfer tax on land sales (Maryland DNR 1979).

When the commission's recommendations were introduced into the legislature, opposition came from two sources. First, real estate developers and brokers argued that the transfer tax would add to the costs of buying and selling property, thus making transactions more difficult. Second, some representatives of local government noted that a state transfer tax would intrude into an area of taxation already being imposed by several local jurisdictions.

The bill survived these objections and became law in 1969, although the program's bond authorization was reduced from $107 million to $60 million. The original legislation limited the program to the acquisition of land, but in 1971 the legislature amended it so that a portion of the funds could also be used for development.

Program Open Space is funded with current revenues generated from the real estate transfer tax. On every real estate transaction in Maryland, a tax of 0.5 percent is imposed. Rapid economic growth in the state and substantial activity in the real estate market since the program was launched have ensured its success. Between 1969 and 1982, the transfer tax generated over $271 million, which was used to acquire over 100,000 acres for state parks, forests, natural environmental areas, natural resource management areas, and wildlife management areas.

The real estate transfer tax was so successful in raising revenue that in 1984 Maryland Governor Hughes suggested amending the legislation to transfer $18 million permanently from the dedicated fund to the state's general fund. Over $42 million had been generated in 1983, reflecting a boom in real estate activity, but opponents were quick to point out that this was an extraordinary year, since the usual figure was between $20 million and $28 million. The governor's proposal was thus defeated because it would have spelled the effective demise of Program Open Space except in years of unusually high real estate activity (Hooton 1984).

The State of Florida

In 1963 the State of Florida established the Land Acquisition Trust Fund (LATF) to provide for expansion of the state park system and to assist local government in acquiring and developing park and recreation areas. This was not a real trust fund: "Trust" merely referred to the fact that the fund was earmarked.

The fund was originally financed by a sales tax on recreational equipment. But in 1968 the revenue source was changed and the recreational equipment sales tax was repealed because it was unpopular with some manufacturers. It was replaced by an excise tax on legal documents that derives about 90 percent of its revenues from real estate transactions. The tax on real estate transactions is based
on the value of property involved in the transaction and currently is assessed at the rate of $4.50 per $1,000 of assessed valuation (Florida Senate 1983).

In fiscal year 1984-85, this tax generated over $300 million. However, only 13.3 percent of this is dedicated to the LATF. The remaining amount is divided 79.5 percent to the General Revenue Fund, and 7.2 percent to the Water Management Lands Trust Fund. Between 1972 and 1983, the documentary stamp tax generated over $170 million for the LATF. By law, the LATF is set aside exclusively for recreational use.

**Implementation by Local Jurisdictions**

In addition to the two states that have implemented a real estate transfer tax to finance park acquisition and development, a number of cities have also adopted it. This section describes its use in Seattle, Washington; a number of Colorado cities; Nantucket, Massachusetts; and San Jose, California.

**Seattle, Washington**

In 1982, Seattle passed an ordinance that imposed an excise tax on the sale of real estate at the rate of 0.25 percent of the selling price. The proceeds from this tax are deposited in the city’s Cumulative Reserve Fund for municipal capital improvements.

The fund is designated for the construction or renovation of city buildings and for the acquisition of real property. Five agencies in the city are eligible to use these funds. They are: the Parks and Recreation Department; Seattle Center, formerly the site of the 1962 World’s Fair; the Library Board; the Seattle Engineering Department; and the Department of Administrative Services, which manages all the municipal buildings except the Parks and Recreation and Utility buildings (City of Seattle Ordinance 110674 1982). The Parks and Recreation Department, according to its Director of Operations, has received about $3.5 million per year from this fund for major capital improvements and repair (Girtsch 1985).

**Colorado Cities**

The search for new sources of income has led a number of Colorado home rule municipalities to adopt real estate transfer taxes. The towns of Avon, Breckenridge, Crested Butte, Gypsum, and Vail and the cities of Aspen and Rifle have enacted ordinances imposing a tax on most transfers of real property (Bauer 1981).

The amount of the tax varies. In Vail, Rifle, and Breckenridge, it is set at one percent of the selling price; in Aspen the rate is 0.5 percent, and in Crested Butte the tax rate is based on the length of time the property has been owned; it ranges from 5 percent if property has been owned less than one year to 0.5 percent if it has been owned from five to ten years; no tax is paid if the property has been owned for ten years or more.

In several of these cities, parks and recreation is designated as a major beneficiary of the revenues generated. For example, in Vail they are used
exclusively to acquire property for parks, recreation, or open space. In Aspen, the funds are designated for the reconstruction and maintenance of the Wheeler Opera House and to provide support for the visual and performing arts. In Crested Butte, the money may be used for public improvement projects that include park, recreation, and open space.

**Nantucket, Massachusetts**

Nantucket Island protects about one third of its 31,000 acres through various government agencies and the Nantucket Conservation Foundation. Still, residents feared that the island's increasing popularity would harm its rustic atmosphere. The number of building permits was accelerating and property values were rising at 15 percent per year (Guenther 1985).

In 1983 residents adopted the idea of establishing a land bank for preserving additional land. Two years later Nantucket issued $10 million in revenue bonds to finance acquisition of beaches and moors threatened by development. The revenue bonds were to be redeemed by a 2 percent transfer tax on real estate transactions. This meant that most current Nantucket residents would not contribute to the land purchase cost. Rather, the bulk of the cost would be borne by people moving onto the island, thereby reducing the amount of open space with their development. The tax received widespread support from real estate brokers and home builders who recognized its contribution to preserving the island's beauty.

**San Jose, California**

San Jose’s Real Property Conveyance Tax is imposed at a rate of $3.30 per $1,000 on all real property transfers within the city. The tax yielded $38 million in the five fiscal years from 1980 through 1985. Park projects are the designated recipients of 64 percent of the revenue, and they actually received $25 million during this time period. Over 90 percent of the tax funds are required to be expended for capital improvements (City of San Jose 1985).

**Mechanics of Implementing the Tax**

At the time title ownership of property is transferred, the responsible party is required to report to the taxing authority the consideration paid for the transfer, the names of the parties, and the location of the property. The specific legislation or ordinance determines whether responsibility for payment of the tax lies with the seller, the purchaser, or both. For example, in the Colorado cities of Avon, Aspen, and Breckenridge, the purchaser is responsible; in Crested Butte and Gypsum, the seller is responsible; and in Vail and Rifle, both the seller and purchaser are responsible.

The agency designated to collect the taxes must be reimbursed out of the receipts for the costs of collection. In Florida, the taxes are collected by the state's 67 county tax assessors and remitted monthly to the Florida Department of Revenue for certification into the LATF. They are compensated by retaining
0.5 percent of the value of the taxes they collect. In Seattle, the King County Comptroller acts as agent for the city in collecting the tax and is permitted to retain one percent of the proceeds collected to defray the costs of collection.

Concluding Comments

The real estate transfer tax is a relatively reliable source of revenue, particularly in those areas with a growing population and an active real estate market. Because land development often decreases recreation opportunities at the same time that it creates need for more recreation areas, it is a very appropriate source of revenue for park acquisition and development. In this respect, its conceptual justification is strong and it is similar to the rationale for mandatory dedication and impact fees. However, there are two important distinctions. First, mandatory dedication is imposed only on the initial development of property, whereas a real estate transfer tax is imposed on each occasion the property title changes ownership. Second, mandatory dedication usually applies only to residential dwellings, while a real estate transfer tax is normally imposed on all types of property transactions.

The ongoing real estate transfer tax imposed rather than the one-time mandatory dedication or impact fee, because recreation and park properties deteriorate with use even when they are well maintained; therefore, they need periodic renovation. Mandatory dedication and impact fees do not provide the ongoing resources needed for such renovation.

Cases can be made for assigning responsibility for the tax to both the buyer and the seller. The seller, as an existing resident, has enjoyed access to the facilities and contributed to their depreciation. Thus, the selling household should contribute to restoring it before leaving. The buyer on the other hand, enjoys immediate access to established recreation and park facilities, but has made no capital contribution to them. This “freeloading” is covered when the buyer contributes through the payment of a real estate transfer tax. An important political consideration in assigning the tax to the buyer is that most of the burden of the tax will fall on existing residents but on newcomers to the jurisdiction. This is particularly likely to occur in areas of rapid growth.

In some instance, both the state and the local agency have imposed a real estate transfer tax. In metropolitan Dade County, Florida, for example, the county uses the tax to finance a loan program for the purchase and rehabilitation of homes for low- and moderate-income people, while the State of Florida levies its own real estate transfer tax to fund the LATF (Lucoff 1983).

The real estate transfer tax incorporates an inherently attractive financial balancing mechanism. The private real estate market is substantially influenced by prevailing economic conditions. Because the real estate transfer tax is tied to that market, the amount of revenue it generates also depends upon economic conditions in the area. However, downturns in the economy do not necessarily reduce its purchasing power, even though funds are reduced as real estate activity slows. Because it would cost less to acquire park land in periods of slow real
estate activity, and because a public agency is likely to purchase in cash, less revenue is needed to purchase desired land. Conversely, when the real estate market is active and land prices are likely to be higher, the tax generates more revenue.

In a growing number of jurisdictions, the real estate transfer tax has provided a valuable source of funds for park acquisition and development. In view of anticipated reductions in traditional funding sources, it seems likely that many other jurisdictions will explore the potential of this revenue source in the future.

References


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