
Coates' Canons Blog: Gentrification and Property Tax Relief

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Downtown Durham is hot. Millions of square feet of new and renovated residential and commercial properties hit the market this year, including luxury condos atop the city's new tallest building. By mid-2020, the number of downtown apartments will have more than doubled and downtown hotel rooms will have more than tripled since 2016.

Further proof of downtown Durham's resurgence is found in the county's 2019 property tax reappraisal. Real property tax values in the city rose more than 20%, with some downtown neighborhoods seeing increases as high as 60%. That growth is on top of the 12% increase produced by the county's 2016 reappraisal.

Charlotte is experiencing a similarly strong real estate market. Real property values increased an average of 53% after Mecklenburg County's 2019 reappraisal, its first since 2011. A large number of properties in downtown Charlotte saw their tax appraisals more than double this year.

While these increases are good news for the cities' financial coffers, they may be problematic for some long-time downtown homeowners. Lower-income residents of the neighborhoods that are experiencing gentrification and rising property values could find it difficult to keep up with their rising tax bills.

Elected officials in both cities heard complaints about their new property tax bills and wanted to take action. Several reached out to the School of Government to ask if their cities could design property tax breaks aimed at residents negatively affected by recent gentrification.

My answer was brief: "Nope." Thanks to G.S. 105-274 and the "uniformity" of classification requirement in the N.C. Constitution, local governments cannot create their own property tax exemptions or modify existing ones to meet their needs. There are already three property tax relief provisions aimed at homeowners: the disabled veterans exclusion; the elderly/disabled exclusion; and the circuit breaker exclusion. All three are limited by income as well as age, disability, or veteran's status. If you are not 65 or older, disabled, or a veteran, you cannot benefit from these tax breaks regardless of how low your income might be.

Local governments of course are free to work with their state senators and representatives to propose amendments to these exclusions or to create new ones aimed at gentrification relief. But they cannot take unilateral action on property tax breaks.

What's more, G.S. 105-380 and -381 severely restrict the authority of local governments to waive property taxes. Taxes can be waived only when they were levied illegally or due to clerical error. Local governments don't have the authority to waive property taxes simply because of concern about the financial status of certain taxpayers.

After hearing this unwelcome news, both cities went back to the drawing board. Working independently, each city developed a grant program to provide direct cash assistance to some low-income homeowners. In late 2017, the Durham council approved a "Longtime Homeowner Grant" program to help with tax increases resulting from the Durham County's recent reappraisals. In 2018, Charlotte City Council approved a similar "Aging in Place" tax assistance program for some taxpayers affected by the 2019 Mecklenburg County reappraisal.

The basic approach to these property tax assistance ("PTA") programs is the same in each city. Both programs offer cash grants, not loans, with no strings attached. Both programs are aimed at low-income homeowners, with the upper income limits set at 80% of the median family income for each city. Both programs require recipients to have lived in their homes for at least five years.

There are some differences between the two PTA programs. Charlotte's program caps its grants at \$1,000, while there is no cap on Durham's grants. Durham's program is aimed only at homeowners in certain neighborhoods who live close to city housing developments, while Charlotte's has no geographic restriction. Charlotte's program is limited to taxpayers who are 65 and older, while Durham's has no age restriction. Durham's grants are paid directly to the homeowners, while Charlotte's are paid to the county property tax collector on behalf of the taxpayer.

Both PTA programs raise the same fundamental question: are local governments authorized to give residents cash to help with their property tax bills? The answer is probably yes, but to get there we need to identify both constitutional and statutory authority for this type of local government action.

Constitutional Concerns

Local governments must demonstrate that their homeowner assistance programs are not unconstitutional gifts of public funds to private individuals. The "emoluments" clause of the N.C. Constitution (Art. I, Sect. 32) prohibits local governments from making payments to private individuals unless those payments are made "in consideration of public services." In other words the public must get something in return for a payment to a private entity. (See this blog post or this one for more on the emoluments clause.) At first glance, PTA programs seem to violate the emoluments clause because they provide direct benefits to private individuals without the cities receiving anything tangible in return.

However, the North Carolina Constitution authorizes local governments to make payments to private parties without receiving any tangible goods or services in return so long as the payments promote a well-established constitutional goal. For example, state-funded loans to college students do not violate the emoluments clause because they promote the well-established constitutional directive to encourage state residents to pursue higher education (N.C. Constitution, Art. IX, Sect. 1).

With the emoluments clause in mind, we need to find a well-established constitutional goal promoted by the PTA grants. There are two likely suspects:

1. Welfare programs for the poor

Providing for the welfare needs of "the poor, the unfortunate, and the orphan" is deemed "one of the first duties of a civilized and a Christian state," according to Section 4 of Article XI of the N.C. Constitution. The state and local governments have for many years operated cash-assistance programs for the poor, including Work First Family Assistance and the Low-Income Energy Assistance Program. If PTA programs could be labeled as welfare programs for the poor, North Carolina courts would likely find them constitutional.

But that result is not guaranteed. It's unclear whether direct cash payments to relatively low-income homeowners would constitute the type of welfare contemplated by the N.C. Constitution. The very few court cases interpreting Art. XI, Sect. 4 all deal with local government funding of medical care for the poor (See for example *Martin v. Wake County*, 208 N.C. 354, a 1935 N.C. Supreme Court case concluding that "care of the indigent sick and afflicted poor is a proper function of the government of this state.") or the building of a county home to house the "aged and infirm." (*Caldwell County v. Sidney Spitzer & Co.*, 173 N.C. 147 (1917)). I was unable to find any N.C. court cases under the welfare provision analyzing cash-assistance programs similar to a PTA program.

Even if such a program were found to fall under Art. XI, Sect. 4, it's possible that a court could find that the income limit chosen by the cities is too high to satisfy this constitutional goal. Federal community development law sets the "low income" limit at 50% of a city's median income, while state welfare law sets it at 60%. The 80% limit chosen by Durham and Charlotte matches the federal definition of "moderate income." Are people of "moderate incomes" considered "poor" in the context of constitutionally authorized welfare programs? Our courts have not answered that question. (More on income limits in the statutory section below.)

2. Affordable housing for low-income persons

The North Carolina Supreme Court long ago approved the constitutionality of subsidies for the creation of affordable housing for low-income persons "when the planning, construction and financing of residential housing is not otherwise

available to 'persons and families of lower income.'" *Martin v. North Carolina Housing Corp.*, 277 N.C. 29, 50, 175 S.E.2d 665, 677 (1970). The court also approved housing loans for persons of moderate income when "private enterprise is unable to meet the need." (See this blog post from my SOG colleague Tyler Mulligan for more on the constitutional and statutory authorization for low-income housing projects.) If PTA programs could be labeled as programs to create or preserve affordable housing for low-income persons, North Carolina courts would likely find them constitutional.

But it is important to note that neither Durham nor Charlotte has taken steps to ensure that the recipients of their PTA grants will continue to maintain them as affordable housing. Under both programs, grant recipients are free to sell their houses to anyone they choose at any time. The buyers might be developers who replace those older affordable homes with expensive new houses or condos. If so, then those grants would have put cash in the pockets of private individuals while doing nothing to help with the constitutional goal of providing affordable housing for low-income residents.

Ideally, PTA programs aimed at minimizing the negative effects of gentrification would include provisions that prohibit grant recipients from selling their homes to anyone other than low-income buyers. One approach would be to require grant recipients to accept deed restrictions requiring that their homes be sold only to low-income buyers as is often done with community land trust property.

Alternatively, PTA payments might be constructed as loans instead of grants. The loans would create liens on the homes that become due and payable only if the recipients sold their houses within a certain time period. After that time period expires, the loans would be forgiven and the liens would be extinguished. This approach would create incentives for recipients to continue to use their homes as affordable housing, perhaps tying the PTA programs to a well-established constitutional goal.

Both these approaches might help solidify the constitutionality of PTA programs but they would also raise some practical concerns. Deed restrictions would lower the market value of the home, due to the smaller universe of eligible buyers. The upside of that change would be lower tax appraisals and tax bills in future years, but the significant downside would be that homeowners would be asked to give away a substantial portion of their home's value in return for grants of a few hundred dollars. Many homeowners would understandably be reluctant to agree to such a deal. If deed restrictions were put in place, who would monitor sales of the affected properties to ensure they satisfied those restrictions? Similar administrative burdens would arise if the PTA program offered loans instead of grants. Who would process the loans and enforce the liens if the grant recipients violate the terms of those loans? While not insurmountable, these approaches do present problems not present with the unrestricted grants offered by the PTAs in Durham and Charlotte.

Interestingly, Durham's tax assistance program was initially proposed as a loan program with restrictions similar to those described above. But a majority of the city council thought it was unfair to ask homeowners to (potentially) pay back the grants when the city routinely offers much larger economic incentive payments to developers without payback requirements. Although comparing economic incentives to PTA grants is a bit like comparing apples to oranges (economic incentives are aimed at jobs and have been explicitly authorized by N.C. courts as explained in this blog post, while neither is true of PTA grants), apparently the council person's arguments carried the day. Durham's tax assistance effort morphed from a loan program to a grant program with no requirement that recipients remain in their homes for any period of time.

Given the complexities and poor alignment with constitutional case law on affordable housing development, the welfare justification seems to be on more solid constitutional ground than the affordable housing justification.

Statutory Concerns

Even if a local government program supports a constitutional goal, that local government needs statutory authority before it may act. (N.C. Constitution, Art. VII, Section 1). The two most likely statutory justifications for PTA programs are the same as those identified in the constitutional analysis above: welfare for the poor and affordable housing for low-income persons.

1. Welfare for the poor

Cities are permitted to spend public funds on programs concerned with the "welfare needs of persons of low and moderate income." G.S. 160D-1311(a)(2). This statute was designed to allow municipalities to take advantage of the federal

Community Development Block Grant (CDBG) program, which defines low income as 50% of area median income and moderate income as 80% of area median income. The Durham and Charlotte programs set their upper income limits at the CDBG's 80% threshold, so presumably they would fall under the federal umbrella for moderate-income housing assistance.

But there are also state income guidelines to consider, and it's not certain exactly how a court might apply them to a PTA program. Another provision of G.S. 160D-1311 authorizes a city council to act as a housing authority under G.S. Chapter 157, which defines "persons of low income" as earning "not more than sixty percent (60%) of the local area median family income as defined by the most recent figures published by the U.S. Department of Housing and Urban Development." Moderate income has a more flexible definition in that statute, but case law regarding assistance for moderate income persons has only extended to loans to encourage the construction of housing for moderate income persons, not welfare grants (See *In re Denial of Single Family Hous. Bonds*, 307 N.C. 52 (1982)).

Counties are also permitted to help the "welfare needs of persons of low and moderate income" but that authorization comes with an important restriction that does not exist in the city welfare statute. G.S. 160D-1311(d) states "No state or local taxes shall be appropriated or expended by a county pursuant to this section for any purpose not expressly authorized by G.S. 153A-149, unless the same is first submitted to a vote of the people as therein provided."

G.S. 153A-149 is the statute that lists the authorized uses of county property tax revenue. That statute does not explicitly authorize welfare programs for the poor. But it does authorize "social services" to "provide for the public welfare through the maintenance and administration of public assistance programs." It seems likely that a court would interpret that provision as authorizing county welfare programs such as a PTA program that pays grants to low income persons. But our courts have yet to wrestle with this question, and as true with many questions surrounding PTAs the answer is far from clear.

2. Affordable housing for low-income persons

G.S. 160D-1311(a)(1) permits cities to spend public funds on "programs of assistance and financing of rehabilitation of private buildings principally for the benefit of low and moderate income persons, or for the restoration or preservation of older neighborhoods or properties." It also allows municipalities to exercise the powers of a housing authority to create housing for low-income persons.

For PTA programs to fall under G.S. 160D-1311, they would need to create or preserve affordable housing for low-income persons. There are two problems with this potential statutory justification.

First, as discussed above, the PTA programs do not require or even encourage recipients to continue using their homes as affordable housing.

Second, even if the PTA grants had restrictions designed to keep low-income homeowners in their homes, it's not clear that paying low-income taxpayers to remain in their homes falls under the scope of G.S. 160D-1311. The statute covers the rehabilitation, restoration and preservation of low-income housing. Those terms could be interpreted as being related only to home improvement and maintenance projects. The PTA grants have no requirement that they be used for such projects. In fact, Charlotte's grants could not be used for such projects because they are paid directly to the county tax collector.

Only if the phrase "preservation of low-income neighborhoods" were interpreted broadly to cover "keeping low-income homeowners in their homes" would G.S. 160D-1311 provide statutory justification for the PTA grants. It is far from clear that a court would adopt such an interpretation.

As Tyler Mulligan explains here, counties possess similar statutory authority to support and promote affordable housing. The county provisions present the same statutory challenges as does G.S. 160D-1311 for cities.

The Bottom Line

Although PTA programs appear at first glance to be affordable housing initiatives, justifying PTA programs under the affordable housing legal rubric raises serious constitutional and statutory concerns. Local governments would be wiser to

justify PTA programs as welfare programs for the poor. The welfare justification is not perfect, given concerns about appropriate income limitations and the statutory limitation on how counties may use their property tax funds. But because local governments and the state have long been involved with similar cash-assistance programs for the poor, it seems likely that courts would also approve of PTA programs under a welfare justification.

Policy Questions

Assuming that PTA programs could pass constitutional and statutory muster, should other North Carolina governments experiencing gentrification follow the lead of Durham and Charlotte and institute their own tax assistance programs?

Local officials need to decide if helping low-income residents with rising property tax bills is the best use of taxpayer dollars. While I can't answer this policy question for local officials, I can offer a few prompts to guide their analysis and discussion. Elected officials and managers intrigued by the programs in Durham and Charlotte might consider how they would answer these potential criticisms:

Why should we pay money to people who are benefiting from rising property values? If they can't pay their taxes, they can sell their now more-valuable homes and move to less expensive neighborhoods.

Why not just lower the property tax rate for all taxpayers instead of using property tax revenue to help pay property tax bills for a lucky few taxpayers? The city council should try to lower the tax burden for all taxpayers rather than create targeted tax relief for some.

For programs that create geographic limits on PTA grants, why shouldn't all low-income homeowners get help with their taxes rather than just those who live in areas seeing lots of growth? Other taxpayers might be struggling with their bills even though their neighborhood is not being gentrified quite as much.

[My colleagues Tyler Mulligan and Kara Millonzi contributed greatly to the analysis above, although any errors or omissions are mine alone. Also note that the statutory references were updated after adoption of the new G.S. Chapter 160D, which recodified many statutes relating to local land use regulations.]

Links

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