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Property Tax Caps: A Look at the Actual Tax Bills of Two Hoosier Homeowners

This November, Indiana voters will have a chance to decide whether they like the recently enacted "tax caps" enough to enshrine them in the state's constitution. Regardless of whether or not voters approve the constitutional amendment, the caps will remain intact as a permanent component of Indiana state law. In other words, voting for the caps will make it harder for them to be reformed by future generations of Hoosiers and their representatives, but will not alter any Hoosier's tax bill today. As a result, Indiana voters should not approve the amendment unless they are completely happy with the caps as they are currently designed.

Deciding whether the caps are so well designed that they are worthy of being written into Indiana's most important document is not an easy task. In an effort to make this task slightly more manageable for Indiana voters, we'll take a look at the actual tax bills of two fairly typical Hoosier homeowners in order to see what lessons can be learned regarding the current property tax system. Ultimately, these examples should make clear that the tax caps leave much to be desired.

Two Real Tax Bills

The details of the 2010 tax bills of two homeowners are contained in the box to the right. These are the actual bills of two employees at the Indiana Community Action Association.

2010 Property Tax Bills for Two Actual Indiana Homeowners

	Property A	Property B
Gross Assessed Value (market value of property):	$ 119,200	$ 176,100
Total Deductions (standard, supplemental, and mortgage deductions):	$ 73,900	$ 93,885
Net Assessed Value (value that is taxed after applying deductions):	$ 45,300	$ 82,215
Tax Rate:	2.2655%	1.9700%
Gross Tax Liability (taxes owed before applying various tax relief measures):	$ 1,026	$ 1,620
State Homestead Credit:	$ 43	$ 48
Local Property Tax Relief:	$ 46	$ -
Total Property Tax Liability Before Cap:	$ 937	$ 1,572
Maximum Allowable Tax Liability Under Cap (1% of Gross Assessed Value):	$ 1,192	$ 1,761
Final Tax Bill:	**$ 937**	**$ 1,572**
Savings From Tax Cap:	**$ -**	**$ -**
Final 2009 Tax Bill:	*$ 955*	*$ 1,471*

Property A is valued at $119,200, while Property B is worth $176,100. The most recent data available (for 2008) indicates that about half of all Indiana homeowners have properties valued at less than $125,000, while half have properties are worth more than this amount. Given this information, the properties examined here are clearly quite typical of those found in Indiana.

Lesson #1: Many Hoosiers Do Not Benefit From the Tax Caps At All

As the shaded area in the box above shows, neither of these homeowners received any benefit from the tax caps in 2010. As they're currently structured, the caps are designed to primarily benefit two groups of people: those living in areas with particlarly high tax rates, and those with very highly valued homes. Neither Property A nor Property B fits into either of these categories. The following two hypothetical examples, created by slightly tweaking the attributes of Properties A and B, can help to demonstrate which types of homeowner might actually expect to benefit from the caps.

Chart 1 alters the math behind each property's tax bill by increasing the tax rate to 2.8%. No other assumptions are changed, though some of the detail contained in the table on the first page has been left out for simplicity's sake. Under a 2.8% tax rate, Property B does actually benefit from the cap, to the tune of $493. Property A, by contrast, still sees no benefit whatsoever from the tax caps, even at this much higher rate. Unfortunately, this result is relatively unsurprising. Homes with higher values (such as Property B) are far more likely to benefit from the cap (and to receive larger benefits) than those homes with lower values (such as Property A).

Chart 1

Hypothetical 2010 Tax Bills Assuming a Higher Tax Rate

	Property A	Property B
Gross Assessed Value (market value of property):	$ 119,200	$ 176,100
Tax Rate:	2.8000%	2.8000%
Total Property Tax Liability Before Cap:	$ 1,179	$ 2,254
Maximum Allowable Tax Liability Under Cap (1% of Gross Assessed Value):	$ 1,192	$ 1,761
Final Tax Bill:	**$ 1,179**	**$ 1,761**
Savings From Tax Cap:	**$ -**	**$ 493**

Another example makes this point even more clear. By returning the tax rates to their actual levels and instead multiplying each home's value by ten, the massive benefits that the tax caps can provide to highly valued homes become even more apparent. In this case, if Property A were worth $1.192 million and Property B were worth $1.761 million, the benefits from the cap would fall in the $5,000 to $6,000 range. ***See Chart 2.*** As this example demonstrates, highly expensive homes receive much larger benefits under these caps than do less expensive homes. And indeed, this is the general consensus among serious researchers that have studied the tax cap regime.

Chart 2

Hypothetical 2010 Tax Bills for Homes Worth Over $1 Million

	Property A	Property B
Gross Assessed Value (market value of property):	$ 1,192,000	$ 1,761,000
Tax Rate:	2.2655%	1.9700%
Total Property Tax Liability Before Cap:	$ 17,189	$ 23,649
Maximum Allowable Tax Liability Under Cap (1% of Gross Assessed Value):	$ 11,920	$ 17,610
Final Tax Bill:	**$ 11,920**	**$ 17,610**
Savings From Tax Cap:	**$ 5,269**	**$ 6,039**

Lesson #2: The Tax Caps Do Not Prevent Your Taxes From Increasing

Many homeowners were a bit confused when they received their 2010 property tax bills in the mail. Despite all the talk about the enormous benefits that Indiana's recent property tax reforms would bring, a large number of homeowners actually saw their taxes rise in 2010 – in some cases by as much as 20% or more. Of the two properties we examined above, one saw its tax bill increase in 2010, while the other saw its bill fall.

Property B, which saw a tax increase in 2010, owes this fact both to the phasing-out of the State Homestead Credit (discussed in more detail under Lesson #3), and to the higher local tax rates it faced in 2010. Property A would have experienced a tax increase in 2010 as well, were it not for the fact that the property's assessed value declined in 2010.

Simply put, while the caps will prevent property taxes from exceeding 1% of your home's value, they will not necessarily prevent increases in your property tax bill because they do not control your homes assessed value and such increases, or increases that may occur in other taxes. As localities struggle under the budgetary pressures inflicted by the recent property tax overhaul, additional surcharges, local income taxes, and voter-approved cap overrides will be sought to fill local budget gaps. And of

course, Hoosier homeowners should not forget that the state sales tax rate increased by 1% to help fund this dramatic restructuring of Indiana property taxes.

Lesson #3: Expect a Tax Hike Next Year

Each property tax form received by Indiana homeowners includes a line labeled "State Homestead Credit," "State property tax relief," or something similar to this. In 2010, the owner of Property A received a $43 tax break as a result of the State Homestead Credit, while the owner of Property B received a $48 break. Unfortunately, the State Homestead Credit program will no longer exist in 2011, and its disappearance will result in tax hikes for a huge share of Indiana homeowners – including the owners of both properties A and B. As with many homeowners, the tax caps are unlikely to protect either Property A or Property B from the tax hike associated with the Homestead Credit's repeal.

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