O'NEILL SCHOOL OF PUBLIC & ENVIRONMENTAL AFFAIRS

Indiana's Property Tax Caps

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Basic Structure

- <u>Not</u> a limit on the rate set by local governments or on their spending.
- Sets a "maximum" bill a property owner can pay after adding up the property taxes owed to the combined property taxing units.
- If the combined bill exceeds the max bill, the difference is just uncollected property taxes for the local governments

Property Tax Bills are Capped as % of Market Value (Gross AV)

- 1% property tax cap for residential homesteads
- 2% property tax cap for non-homestead households and agriculture
- 3% on everything else (commercial, industrial, etc.)

1% Residential Homestead Vs. 3% Property

	1% Homestead	3% Commercial
Market Value→	$150,000	$150,000

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Market Value→	$150,000	$150,000
Taxable Value→	$65,250	$150,000

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Max Bill→		

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Max Bill→	$1,500	$4,500

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Market Value→	$150,000	$150,000
Taxable Value→	$65,250	$150,000
Max Bill→	$1,500	$4,500
Rate Needed to Cap→		

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Max Bill→	$1,500	$4,500
Rate Needed to Cap→	2.3%	3%

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Tax Bills > Than

Taxpayer Perspectives: 3 points

1. **Reduces exposure** to swings in property tax bills **caused local governments increasing their taxes**.

2. Once your bill is at the max, spending/debt financed by property taxes are "free"

3. **Increases exposure** to swings in property tax bills **caused by property value increases.**

Local Government Perspectives: 4 points

1. Property Tax Caps are Structural Deficits:
   - Property tax bills not paid due to the caps are uncollected revenues **after** spending choices are approved. To cut $1 of property tax cap losses requires much more than $1 reduction in expenditure budget.
2. Overlapping local governments are incentivized to raise property tax rates and other taxes
   - The paid portion of the tax bill is distributed to each unit as a fraction of the payer's total tax rates

Local Government Perspectives: 4 points

3. Creates a class of property taxpayers who benefit from services but don't pay the additional cost (creates pro-spending bias)

4. Mixed incentives on development

   – Residential housing is capped at lower rates, an incentive to favor more non-residential development

   – Big incentive to just get more total AV development

Administrative/Legal Challenges

1. Assessment records need to allow for mixed “cap use”
   - E.g. A farm can have a family home (1%), farmland for crops (2%), and a retail shop to sell directly to consumers (3%)
2. Lots of “edge cases” on cap classifications
   - E.g., is an assisted living facility for seniors who pay rent subject to commercial (3%) or non-homestead residential (2%) cap?
3. Lots of non-uniformity in taxation (two properties of equal value get different tax bills based on use), Indiana had to amend the constitution to allow

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Property Taxes Are Not Like Other Taxes

- Other Taxes: 1) Government Sets a Rate; 2) People buy/sell under the rate to create tax revenue; 3) Government spends the Revenue

- Property taxes: 1) Government sets the budget for spending; 2) property tax rates are calculated using taxable values; 3) individual taxpayers use the rate to determine their share of the budget

- ***Taxable values are used to determine how to divide the cost of governments' spending into individual tax bills***

- ***The property tax caps mean that not everyone has to pay their share of the bill***

Demonstration (same class different AV)

2 RH taxpayers with $190,000 Net AV and Levy of $3,800 (implies 2% property tax rate)

	Taxpayer A	Taxpayer B
Gross AV	$100,000	$200,000
Net AV	$45,000	$145,000
Gross Tax Bill @2%	$900	$2,900

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