

Estimating 2009 Circuit Breaker Credits: A 12-Step Guide for Indiana Local Governments

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Indiana's 2008 property tax reform complicates the local government budget process. In the past it often was possible to estimate the effect of tax rate, levy or assessed value changes by simply recalculating aggregate numbers. With the new circuit breakers, however, estimates of the amount of revenue governments will receive in 2009 require parcel-by-parcel data by taxing district and property type.

This will add a new step to the budget process, an estimate of the circuit breaker credits likely to be received by each taxpayer in the county. There are no real experts in how this will be done. This paper outlines the steps I've used in past efforts at property tax modeling, in the State House, and using data provided by Fayette County. By the end of the 2009 budget process, however, local officials will be the experts.

Estimating Taxing District and Government Unit Net Assessed Values

1. *Acquire gross assessed value and deduction data.* Needed are parcel-by-parcel gross assessed values and deductions for 2008 pay 2009, labeled by tax district and property type. Parcels should be identified by real property categories, including residential homesteads, residential non-homestead rentals, residential other, agricultural homesteads, agricultural land, agricultural other, commercial long-term care facilities (retirement and nursing homes), commercial apartments, and all other real property (commercial other, industrial, utility). Personal property may be aggregated into a single category.

Notes:

- 2008 pay 2009 gross assessed value data may not be available when it's needed. Projections from 2007 pay 2008 data may have to be used. Projections could be based on past local trends and knowledge of particular property changes. The farm land base rate has increased from \$1,140 to \$1,200 from 2007-08 to 2008-09, so agricultural land assessments may be increased by 5.26%.
- Some parcels have homestead and non-homestead gross assessed value. The tax payments from these types should be computed separately, so the homestead deductions and credits need to be split from the non-homestead deductions and credits.
- HEA 1001, Section 221, defines "residential" property to include non-homestead single family homes, buildings with two or more dwelling units, the land shared by these units, and land rented for a mobile home. All of this property is eligible for a 2.5% circuit breaker credit in 2009 (and 2% in 2010). Note that the circuit breaker definition of residential includes commercial apartments. However, for the property tax relief local option income tax, relief can be distributed to homesteads and other "qualified residential property", which is apartments and residential rentals (IC 6-1.1-20.6-4 and -5), but not second homes or vacation homes. If the county has or might consider a LOIT that uses the qualified residential distribution, residential gross assessed value should be divided into homesteads, residential rentals and other. Where this is not possible, LOIT distributions must be estimated based on all non-homestead residential property.
- Counties have the assessment and deduction data required to do this analysis. It's the same data used to calculate tax bills—in fact, this analysis is essentially a simulated tax billing. However, in some counties the data may not be in the form needed for analysis. The data that counties or their vendors send to the Department of Local Government Finance (DLGF)

includes the data required to do this analysis. It is this data that the Legislative Services Agency (LSA) uses to do statewide analyses of circuit breakers. Any county can request its own data from LSA (though not LSA's analysis). For some counties this may be the easiest way to acquire the necessary data.

2. *Subtract deductions from gross assessed value.* HEA 1001 changes the homestead deductions for taxes in 2009. The maximum homestead standard deduction has increased from 50% to 60% of homestead gross assessed value, up to \$45,000. A new supplemental homestead deduction has been added, equal to 35% of homestead gross assessed value, after the standard deduction is subtracted, up to \$600,000. The deduction is 25% of assessed value above \$600,000.

Calculate the maximum of \$45,000 or 60% of homestead gross assessed value, and subtract this from homestead gross assessed value. If this remainder is \$600,000 or less, multiply by 35% for the new supplemental homestead standard deduction. If this value is above \$600,000, take \$210,000 (=35% of \$600,000) plus 25% of the amount above \$600,000. Subtract this supplemental deduction from homestead gross assessed value. Subtract existing deductions from the gross assessed values of the remaining parcels.

Notes:

- HEA1001 makes big changes in homestead deductions. The homestead deductions must be calculated using the new formulas. Other deductions are unchanged. Some of these are fixed (like the mortgage deduction), others are a percentage of gross assessed value (like commercial/industrial tax abatements), and some have elements of both (like the \$12,480 or 50% of gross assessed value maximum on the 65 and over deduction). If possible the deduction amounts should be recalculated based on the deduction formulas, with the projected gross assessed values. If this is not possible, current year deduction amounts can be used. If assessments are projected to rise slowly, this will understate deductions by a small amount, and overstate circuit breaker credits by a small amount.

3. *Calculate tax district and unit net assessed values.* Sum parcel-by-parcel net assessed values from step 2 by tax district. Sum the tax district assessed values that comprise each unit's net assessed value.

Calculate Government Unit and Taxing District Tax Rates

4. *Acquire the proposed tax levies by unit and fund.* Civil units are required to submit these proposed levies to the county council at least 15 days before final budgets are adopted. In 2009 several levies will be taken over by the state, including the school general fund levy, the special education pre-school levy, the county welfare levies, and the pre-1977 municipal and township police and fire pension levies, and the part of property tax levies used for incarceration of juveniles in state corrections facilities. The state levies will be eliminated as well.

Notes:

- Section 148 of HEA 1001 requires civil taxing units to file their proposed tax rates, levies and budgets with the county council in advance of budget adoption. School corporations are not included in this requirement. In counties likely to have significant circuit breaker credit losses, however, it should be in the interest of the school corporations to participate. They too will need an estimate of their circuit breaker losses for budgeting purposes. If school corporations do not participate, their levies will need to be estimated, perhaps based on past levy trends.

- In counties that adopt the levy freeze local option income tax for 2009, levies for civil government operating funds will not change from 2009. Civil governments do not include school corporations. Operating funds do not include debt service and cumulative funds.
- Cities, towns and townships sometimes have a levy specifically for the pre-1977 police and fire pensions. Sometimes these appropriations are included in other funds. HEA1001 requires that the local unit's tax levy be reduced by the pre-1977 police and fire pension locally-financed appropriation, in whichever fund they are placed.
- There are dozens of cross-county units in Indiana. These are municipalities, school corporations, library districts and other special districts that are in more than one county. The projected tax rates for these units will be needed for the circuit breaker credit analysis. Cross-county units are required to file their tax and budget proposals only with the county in which they have the greatest assessed value. Other counties that share these units will have to request this information from the units' main county, or project the cross-county units' tax rates based on past trends.

5. *Calculate unit-fund tax rates.* Divide the proposed fund levies (less the state takeovers) from step 4 by the unit net assessed values from step 3. Multiply by 100 to obtain the new tax rates, in dollars per \$100 assessed value.

6. *Calculate tax district tax rates.* Sum the proposed unit-fund rates by taxing district.

Notes:

- In Lake and St. Joseph Counties, debt service levies are not subject to the circuit breaker limits. Each taxpayer's non-debt service levy must be calculated to estimate the circuit breaker credits. The district tax rate should sum only the non-debt service rates in these two counties.
- Construction projects passed by referendum are not subject to the circuit breaker limits. In some counties there may be such referenda on November 2008 ballots. If the referendum passes, the tax rate will not be included in the tax district rate used to calculate circuit breaker credits, since the debt service is outside the circuit breaker limits. If the referendum does not pass, then there will be no added debt service rate in 2009. Thus, November referenda rates can be ignored in the 2009 circuit breaker credit calculation.

Calculate Parcel Tax Bills

7. *Calculate parcel gross tax bills (before state and local credits, if any).* Multiply the 2008 pay 2009 net assessed values for each property parcel (from step 2) by the tax rates for the appropriate tax district (from step 6). Divide by 100 to obtain estimated gross tax bills, before credits.

8. *Calculate parcel credits and net tax bills, before circuit breaker credits.* HEA 1001 eliminates property tax replacement credits and traditional state homestead credits in 2009, so these percentages should not be subtracted. Estimate the county's dollar share of the \$140 million in added homestead credits provided for 2009 by HEA1001. This can be done using the county's percentage share of the 2008 \$620 million from DLGF's April 29 memo. Divide this total by the sum of gross tax bills of homesteads to get the homestead credit percentage. Multiply this percentage by homestead gross tax bills to get the dollar credit, and subtract the credit from the homestead gross tax bills.

Calculate credits from local option income taxes. These may include the COIT local homestead credit, the EDIT homestead credit to offset inventory tax shifts, and the LOIT credit for property tax relief. Calculate local credit percentages, and subtract from the tax bills of the parcels that receive the tax relief.

COIT homestead credits apply only to eligible levies, essentially non-debt service levies. The eligible share can be estimated for each taxing district by adding the tax rates of the eligible funds (essentially the operating rates), and dividing by the total district rate. This share times the COIT rate passed in the ordinance is the estimated COIT homestead credit rate to be applied to homesteads in each taxing district.

The calculation of the EDIT homestead credit to offset inventory tax shifts will have to change, now that HEA1001 has exempted inventories from assessment (rather than providing a 100% deduction from assessments). New data on inventory assessments will not be available. The most recent year's inventory assessment data will have to be used. Calculate the credit based on the difference between what homesteads would have paid had inventory assessments been included in assessed value, and what they will actually pay.

The credit rate for the LOIT for property tax relief can be estimated by dividing the total LOIT revenue (estimated from existing local income tax revenues) by the sum of the tax bills of the parcels eligible for the tax relief. This sum depends on the distribution of the LOIT tax relief. Divide LOIT revenue by the sum of homestead tax bills if only homesteads will receive relief. Divide LOIT revenue by the sum of homestead and rental housing tax bills if these parcels are to receive relief. Or, divide LOIT revenue by the sum of all tax bills if all taxpayers will receive relief.

Notes:

- The county's share of the state homestead credit will change year-to-year, as the county's share of statewide homestead gross tax bills changes. The change may be particularly large in 2009, because of the elimination of school general fund levies. Counties where these levies are a large share of total levies will have a smaller share of statewide homestead tax bills in 2009 than they did in 2008. Until the actual 2009 shares are known, however, the 2008 share provides the best estimate.
- Subtract the state homestead credits from the gross tax bills *before* calculating the LOIT credit for property tax relief. This won't matter if the LOIT relief is distributed only to homesteads. If it goes to homesteads plus other kinds of property, subtracting the state homestead credits first will mean a slightly higher share of the relief will go to non-homestead property.

Calculate Circuit Breaker Credits by Parcel, Taxing District and Government Unit

9. *Calculate the circuit breaker tax bill limits.* Assign the appropriate circuit breaker percentage to each parcel: 1.5% for homestead property, 2.5% for other residential (including commercial apartments), farm land and nursing homes, and 3.5% for all other property (including personal property). These are the rates for 2009. Rates for 2010 will be 1%, 2% and 3%, respectively. Multiply these percentages by the gross assessed value of each parcel.

Notes:

- Some parcels include both homestead and non-homestead property. The circuit breaker limits should be calculated separately for the two property types. If this is not possible, add the limits on the homestead and non-homestead property to get an overall limit for the parcel. This will lead to an underestimate of circuit breaker credits, but this underestimate will be small if there are not many parcels have both homestead and non-homestead property, or if the non-homestead share of the parcel AV is small.

10. *Estimate the circuit breaker credits by parcel.* Compare the estimated tax bills (step 8) to the circuit breaker tax limits (step 9). Where the tax bill exceeds the circuit breaker limit, subtract the tax limit from the tax bill. These are the circuit breaker credits received by taxpayers. Where the tax bill is less than the tax limit, the circuit breaker credit is zero.

Notes:

- Again, some parcels include both homestead and non-homestead property. The circuit breaker credits should be calculated separately for the two property types, if possible.
- In Lake and St. Joseph Counties, debt service levies are outside the circuit breaker limits. The tax bill eligible for the circuit breaker credit should be calculated using the district non-debt-service tax rates from step 6. Compare the eligible tax bill to the circuit breaker limits to calculate the circuit breaker credits.

11. *Estimate the circuit breaker credits by tax district.* Sum the parcel circuit breaker credits from step 10 by tax district.

Notes:

- Counties may want to do a separate sum of circuit breaker credits by property type—homestead, other residential plus farm land plus retirement homes, and all other real and personal property. This can be useful in the local option income tax adoption decision.

12. *Estimate the circuit breaker credits by unit and fund.* Distribute the tax district circuit breaker credit sums among units and funds based on the shares of each unit-fund tax rate in the total district tax rate. Sum the unit-fund circuit breaker credits for each unit. These are the circuit breaker revenue losses for each local government unit.

Notes:

- Debt service funds will show losses in this calculation, but HEA 1001 requires debt service payments to be fully funded (the bondholders insist!). This means that the circuit breaker revenue losses will be allocated among the non-debt service funds.