Crunching Indiana Tax Reform

Looks like we’re going to have quite a debate about Indiana taxes in 2002. The state budget is $1.3 billion in the red. There’s a property tax reassessment. The governor proposed a plan to restructure taxes.

Everyone is concerned about the well being of our state. But just about everyone also is concerned about an issue closer to home. After all the tax changes, will I pay more or less than I pay now?

Let’s crunch some numbers, figure out how the taxes of a Hoosier household would change. Now, no one is typical, but according to the Census, there are an awful lot of households meeting this description: homeowner, income around $50,000, family of four with two children. It might be that family down the street—you know, the O’Kernans, Joe and Fran, and their kids, Jeff and Vi.

It’s none of our business, but let’s figure how much the O’Kernans paid in state income taxes this year. Take that $50,000, subtract the personal deductions at $1,000 a head, the child deductions at $1,500 each and their property tax payment, $1,041. Their taxable income is $41,959. As any calculator will tell you, at the current tax rate of 3.4 percent, that’s $1,427. The governor’s tax restructuring plan raises the rate to 3.9 percent for incomes under $90,000, and raises the child deduction to $2,000. The O’Kernans would pay $1,597, an increase of $170.

The sales tax is tougher. How much does this family spend on taxable items? The U.S. Bureau of Labor Statistics provides some numbers from its survey on consumer spending. A family of four with this income spends a little more than $19,000 a year on things that Indiana taxes. At 5 percent, the sales tax payment is $954. Bet the O’Kernans have no idea that all those nickels add up to that much! The rate under the governor’s plan is 6 percent. The O’Kernans would pay $1,131, a $177 increase.

The property tax is the toughest of all. Reassessment will increase the assessed value of almost everyone’s house, but will decrease almost everyone’s property tax rate. The average Indiana house sells for about $100,000. Its assessed value under the current rules averages about $13,300. The average Indiana tax rate is $8.70 per $100 assessed value, which means a payment of $1,157. Except there’s a 10 percent homestead credit, which cuts the payment to $1,041.

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Now, under the new rules, property will be assessed at its market value, less a shelter allowance of around $19,000. That and existing deductions reduce taxable assessed value to $70,400. The average tax rate will fall to around $1.69 per $100 assessed value. Because assessed values are up, tax revenue is controlled, and the tax proposal cuts the property tax levy by about a billion dollars. It also increases the homestead credit to 15 percent. Put it all together, and the O’Kernans pay $1,011, $30 less than they pay now. With this smaller property tax payment, they have a smaller income tax deduction, so their income tax payment goes up another $3.

There are other things that we could consider. There are new tax breaks for renters and low-income people that the O’Kernans can’t use. Their federal tax liability would drop if they itemize their state income and property taxes. The plan cuts some business taxes, like the property tax on inventories, so the O’Kernans would benefit from prices lower—and job opportunities greater—than they would have been.

How does our household make out? They pay $30 less in property taxes, $173 more in state income taxes and $177 more in sales taxes. That’s a tax increase of $320. But wait! The Indiana courts say that we must change our property tax system. What the O’Kernans pay now must change. Market value assessment would satisfy the courts. If we made no other changes, they’d pay about $350 more. Compared to that, under the governor’s plan the O’Kernans save $30.

Some think the best comparison is to what households pay now. Some think the best comparison is to what they would pay if the tax plan were not adopted. You’ll hear both numbers during the coming debate. Keeping them straight is not going to be easy.

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