

TAX FACTS



Taxpayers' Federation of Illinois

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Homestead Exemptions: Shifting Tax Burden, But Not Cutting Taxes

By Mike Klemens

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Illinois saw an unprecedented decline in property values over the last four years, but property owners saw their tax bills continue to rise. Amidst all of this up and down, homeowners did get a break because their homestead exemptions – generally fixed dollar amounts subtracted from their homes' declining values – shielded from taxation an ever-larger portion of their assessment. However, what homeowners saved was shifted on to owners of non-homestead properties.

Declining Values/Rising Taxes

The last four years have been unique in the complicated world of Illinois property taxation. The bursting of the real estate bubble wiped out almost one quarter of the property tax base between 2009 and 2013 (taxes payable in 2010 and 2014). At the same time property taxes billed (extended) grew 7.4 percent. **See Table 1.** Little wonder that property taxes bewilder citizens

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NOTES FROM THE INSIDE. . .

By Carol S. Portman

In this edition of *Tax Facts*, we shift from our usual in-depth tax policy articles and instead offer a pair of shorter pieces on more timely issues. In the first, we follow up on a detailed 2014 analysis of the Illinois homestead exemption to make a couple of points. First, when housing values plummeted during the real estate crash, homestead exemptions became more valuable as they took up a greater portion of home value.

The second point that we make is that in the property tax world, the homestead exemptions – indeed all exemptions – don't reduce property taxes. Exemptions require higher tax rates and shift taxes from homeowners onto owners of rental, commercial, and industrial property. And, even the homeowner with the exemption pays a higher tax rate on the taxable portion of their property.

The second article deals with the classification system in Cook County, which shifts tax burden off residential property and onto commercial and industrial property. A study by the Lincoln Institute of Land Policy and TFI's equivalent agency in Minnesota, the Minnesota Center for Fiscal Excellence, looks at property taxes in three Illinois communities. Of the three, Chicago homeowners pay the lowest effective tax rate, while Chicago commercial property owners pay the highest effective tax rate.

The study also takes a unique look across the states, measuring the extent to which property tax burden is shifted from homeowners onto commercial properties in the largest city in each state. Chicago has the seventh highest rate of shift off homeowners and onto commercial property. Overall, Illinois is a high property tax state, but, because of classification, the taxes paid by a Chicago homeowner are only slightly above the national average, while commercial property taxes are third highest in the county.

who watched their property values plummet while their property tax bills rose.

TABLE 1. Illinois EAV and Taxes Billed, 2009 - 2013

Year	Equalized Assessed Valuation	Total Taxes Extended
2013	303,048,928,342	27,128,941,225
2012	321,073,431,554	26,766,182,466
2011	348,071,849,473	26,187,486,829
2010	377,321,501,247	25,915,360,351
2009	392,939,664,165	25,260,324,314

Source: Illinois Department of Revenue, *Property Tax Statistics*

When property values and assessments are falling, the fixed-amount homestead exemption benefits homeowners because the homestead's relative share of total assessed value declines. While the homeowner benefits, what they save is simply shifted onto non-homestead properties, i.e. businesses and residential rental properties.

To put numbers on it, in 2011 (the first year that Cook County's Adjusted General Homestead Exemption did not skew statewide numbers) homestead exemptions represented 12.8 percent of residential equalized assessed value. In 2013, largely due to declining assessments, that had risen to 14.1 percent.

Example

To see the effect of the shift that homestead exemptions cause, take a hypothetical taxing district that has just two identical houses, one

owner-occupied and one rental. Each has an EAV of \$100,000. If the taxing district sets a levy of \$16,000, the resulting tax rate will be 8 percent and each property will pay \$8,000.

Now, give the owner-occupied property a \$10,000 homestead exemption. The tax rate needed to produce the \$16,000 levy increases to 8.421 percent (\$16,000/\$190,000). The homestead property will pay \$7,579 and the non-homestead property will pay \$8,421. See **Table 2**.

In this simplified example, the \$421 savings for the homestead property (\$8,000 - \$7,579) is shifted onto the rental property (\$8,000 vs \$8,421), in a direct shift. In a real taxing district

the amount of the shift would be much more complex. The exact amount of the shift would depend upon the taxable value of the non-homestead properties; the greater the relative share of non-homestead properties available to carry the higher rate, the greater the value of the exemption to the homestead properties.

Hidden Shift

And then there is the hidden shift. The homestead exemption drives up the tax rates, including the rate that applies to the portion of the home's assessment not covered by the homestead exemption. Looking to our example above, the homestead property pays no tax on \$10,000 of its EAV, but pays a higher tax rate on the remaining \$90,000. Most homeowners would figure their savings by multiplying the

\$10,000 homestead exemption by the 8.421 percent rate, or \$842. As we identified above, the real savings was \$421.

Conclusion

In the property tax world, giving exemptions to one type of property simply shift taxes onto other property owners. This is true whether the exemption is for a

TABLE 2. Homestead Exemptions and Tax Shifts				
	No Homestead Exemption		With Homestead Exemption	
Taxing District Levy	\$16,000		\$16,000	
Taxing District EAV	\$200,000		\$190,000	
Tax Rate	8.00%		8.421%	
	Rental	Homestead	Rental	Homestead
Parcel EAV	\$100,000	\$100,000	\$100,000	\$100,000
Homestead Exemption	\$0	\$0	\$0	\$10,000
Taxable Value	\$100,000	\$100,000	\$100,000	\$90,000
Tax Rate	8.00%	8.00%	8.421%	8.421%
Tax Bill	\$8,000	\$8,000	\$8,421	\$7,579
Real Shift - Savings/ (Cost) with Homestead Exemption			(\$421)	\$421

Source: Calculations by author

new industrial plant, for a hospital, or a homestead exemption. There's no free lunch with property tax exemptions; somebody pays.

Endnote: For a detailed discussion of the homestead exemptions available in Illinois, see Tax Facts Summer 2014, "Homestead Exemptions: Confusing, Complicated and Costly." While there have been a few changes to

the exemptions (increasing amounts and expanding availability) since the article was written, the 2014 analysis and summary remain accurate. The current proposal to raise Chicago property taxes to cover unmet police and fire pension liabilities includes a proposal that will add to the confusion and complexity by (1) doubling the homestead exemption in a portion of a county and (2) only applying the higher exemption to a portion of the tax bill.

How Classification in Cook County Compares with Other States

By Mike Klemens

Mike Klemens, President of KDM Consulting Inc., does tax policy research for the Taxpayers' Federation.

Illinois is a relatively high property tax state. This is not news, but is reaffirmed by many studies, including the "50-State Property Tax Comparison Study" conducted annually by the Minnesota Center for Fiscal Excellence and the Lincoln Institute of Land Policy. More significantly the study also illustrates differences within Illinois caused by the Cook County classification system that shifts property tax burden from homeowners onto commercial and industrial property. The latest study, done for taxes payable in 2014, shows that residential taxes in Chicago are near the average for the largest city in other states, while Chicago's commercial and industrial property taxes are among the highest.

The Study's Basic Methodology: The "50-State Property Tax Comparison Study" calculates effective tax rates for four property classes: homestead, commercial, industrial and apartment property in the largest city in each state and the District of Columbia. For Illinois and New York, because Chicago and New York City differ from the rest of the state, the study also calculates effective tax rates for the second largest city (Aurora in the case of Illinois). The study also evaluates a rural community in each state (Galena in Illinois' case).

This methodology allows comparison of property taxes in Chicago, Aurora, and Galena to comparable cities in other states and to each other. To determine the effective tax rate, the

property tax owed divided by market value, researchers select specific values of property, take into account the level of assessment, apply generally available exemptions, make assumptions about amounts of personal property, and apply the relevant tax rates to the properties.

Here are some highlights:

Homestead Property Taxes \$150,000 Property			
Urban			
Rank	City	Net Tax	Effective Tax Rate
3	Aurora	\$5,210	3.473%
18	Chicago	\$2,438	1.625%
	Urban Average	\$2,235	1.490%
Rural			
	Galena	\$3,071	2.047%

see much higher taxes on their homes than their neighbors in the City. With commercial and industrial properties in the City, the reverse is true: Chicago's taxes are higher than other Illinois communities, although both City and suburbs are ahead of the national average.

Commercial Property Taxes \$100,000 Property			
Urban			
Rank	City	Net Tax	Effective Tax Rate
3	Chicago	\$46,323	3.860%
6	Aurora	\$39,307	3.276%
	Urban Average	\$25,883	2.157%
Rural			
	Galena	\$23,263	1.939%

Industrial Property Taxes \$1,000,000 Property			
Urban			
Rank	City	Net Tax	Effective Tax Rate
12	Chicago	\$40,558	2.028%
14	Aurora	\$39,307	1.965%
	Urban Average	\$31,536	1.577%
Rural			
	Galena	\$23,263	1.163%

Apartment Building Property Taxes \$600,000 Property			
Urban			
Rank	City	Net Tax	Effective Tax Rate
4	Aurora	\$23,584	3.744%
23	Chicago	\$11,338	1.800%
	Urban Average	\$12,211	1.938%
Rural			
	Galena	\$13,598	2.215%

The results of this part of the study parallel what we've seen in countless others: Chicago homeowners and renters pay property tax that is not much different from the national average, while rural and especially suburban residents in Illinois

Measuring the Effects of Cook County's Classification System

The study also calculates the rate of commercial subsidization of homeowners in each urban city in its study. It does this by dividing the Effective

Tax Rate calculated for a \$1 million commercial property by the Effective Tax Rate for the median valued homestead in each of the 53 jurisdictions. A ratio of 1.0 would mean there is no subsidization. A ratio above 1.0 means that commercial property is subsidizing homesteads; the higher the number the greater the subsidy. A ratio below 1.0 means that homeowners are subsidizing commercial property. The results are set forth in Table 19 from the study on page 7.

On average for the 53 cities the ratio is 1.71, which means that some subsidization is common and that on average commercial properties pay taxes at a rate 71 percent greater than the typical homeowner. Reasons for this vary, but here is how the authors of the study explained the shift:

Differences in the quality of assessments among various classes of property can produce a de facto classification system even in the absence of statutory classification schemes. Locations that rank near the top of this list do so because of extreme differences in classification ratios between these two types of property. For instance, in New York City, residential property is assessed at 6% of value while

commercial property is assessed at 45% of value. In other cases differences in tax rates and/or homestead exemptions or credits account for the differences, such as in Boston; where nearly 37% of the value of the median home is exempt from taxation and the homestead tax rate is some 40% that of commercial and industrial properties.

For Chicago the ratio is 2.696, eclipsing the national average as the seventh highest subsidization ratio. This is almost entirely due to the 2.5-to-1 differential statutorily mandated by Cook County’s classification system. For Aurora, located in Kane County, the ratio is 1.123. The availability of homestead exemptions almost certainly explains why Aurora’s ratio is slightly above 1.0, and Chicago’s is above 2.5.

The complete study contains many additional interesting tidbits about property taxes nationwide, and is available at http://www.lincolnst.edu/pubs/3550_50-State-Property-Tax-Comparison-Study.

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Illinois Tax Facts

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TABLE 19. Ratio of Relative Subsidization of Homeowners by Commercial Property

State	City	Median Home Value (\$)	Ratio	Rank
New York	New York City	488,100	4.323	1
Massachusetts	Boston	381,700	4.009	2
Hawaii	Honolulu	550,400	3.663	3
South Carolina	Columbia	163,600	3.661	4
Colorado	Denver	263,900	3.618	5
Indiana	Indianapolis	116,400	3.125	6
ILLINOIS	Chicago	211,400	2.696	7
Louisiana	New Orleans	183,100	2.382	8
Arizona	Phoenix	162,300	2.355	9
Alabama	Birmingham	83,800	2.200	10
Kansas	Wichita	115,800	2.173	11
Pennsylvania	Philadelphia	136,800	2.170	12
Minnesota	Minneapolis	179,900	2.157	13
Idaho	Boise	169,000	2.093	14
West Virginia	Charleston	107,000	2.071	15
D.C.	Washington	470,500	2.028	16
Iowa	Des Moines	113,900	1.962	17
Rhode Island	Providence	170,800	1.909	18
Mississippi	Jackson	84,000	1.874	19
Missouri	Kansas City	126,900	1.831	20
New York	Buffalo	68,500	1.791	21
Utah	Salt Lake City	249,600	1.788	22
	U.S. Average		1.710	
	U.S. Average (w/o NYC)		1.659	
Tennessee	Memphis	89,400	1.600	23
Montana	Billings	186,600	1.481	24
Florida	Jacksonville	129,700	1.452	25
Ohio	Columbus	123,700	1.365	26
South Dakota	Sioux Falls	153,300	1.341	27
Texas	Houston	125,700	1.330	28
Arkansas	Little Rock	159,900	1.262	29
Georgia	Atlanta	200,900	1.256	30
North Dakota	Fargo	164,200	1.203	31
New Mexico	Albuquerque	183,400	1.153	32
ILLINOIS	Aurora	159,300	1.123	33
Vermont	Burlington	273,900	1.104	34
Michigan	Detroit	36,800	1.086	35
Alaska	Anchorage	295,500	1.079	36
Oklahoma	Oklahoma City	136,900	1.071	37
Wisconsin	Milwaukee	113,900	1.065	38
Maine	Portland	230,000	1.045	39
Wyoming	Cheyenne	197,800	1.036	40
California	Los Angeles	451,200	1.016	41
Kentucky	Louisville	141,900	1.014	42
Nebraska	Omaha	134,600	1.000	43
New Hampshire	Manchester	206,600	1.000	43
New Jersey	Newark	206,200	1.000	43
North Carolina	Charlotte	165,900	1.000	43
Oregon	Portland	291,400	1.000	43
Washington	Seattle	436,600	1.000	43
Nevada	Las Vegas	162,400	0.988	49
Delaware	Wilmington	152,100	0.981	50
Virginia	Virginia Beach	259,200	0.953	51
Connecticut	Bridgeport	163,400	0.868	52
Maryland	Baltimore	150,000	0.862	53

Source: 50-State Property Tax Comparison Study, Lincoln Institute of Land Policy and Minnesota Center for Fiscal Excellence

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