



## **The Erosion of the Homestead Tax Credit** Value of Property Tax Relief Lessened by Effects of Inflation

The Homestead Tax Credit delivers property tax relief to low-income owners and renters. For years, the formula for calculating the Homestead Credit was the only major part of the tax code that was not indexed to account for the effects of inflation. As a result, the real value of the credit and the total amount of the credits has dropped.

The 2009-11 biennial budget addressed the issue of inflation by requiring that the state index the factors figuring into calculating the credit. The Governor's 2011-13 budget proposes repealing the indexing requirement, which would save \$3.1 million in fiscal year 2012 and \$10.5 million in 2013.

### **About the Numbers**

With the exception of the dollar amounts noted above, which are from the Legislative Fiscal Bureau (Budget Paper # 605), the figures in this report are taken from Department of Revenue publications, and the amounts are adjusted for inflation.

### **About the Homestead Tax Credit**

The purpose of the Homestead Tax Credit is to make property taxes less burdensome for low-income households in Wisconsin. As a circuit breaker-style credit, the Homestead Credit uses a formula to insure that households pay no more than a set percentage of their income in property taxes.

Relief takes the form of a credit that reduces individual income tax liability. The Homestead Tax Credit is refundable, which means that if the credit is more than the filer's tax liability, the state cuts the filer a check for the difference.

### **Inflation Has Eroded the Value of the Credit**

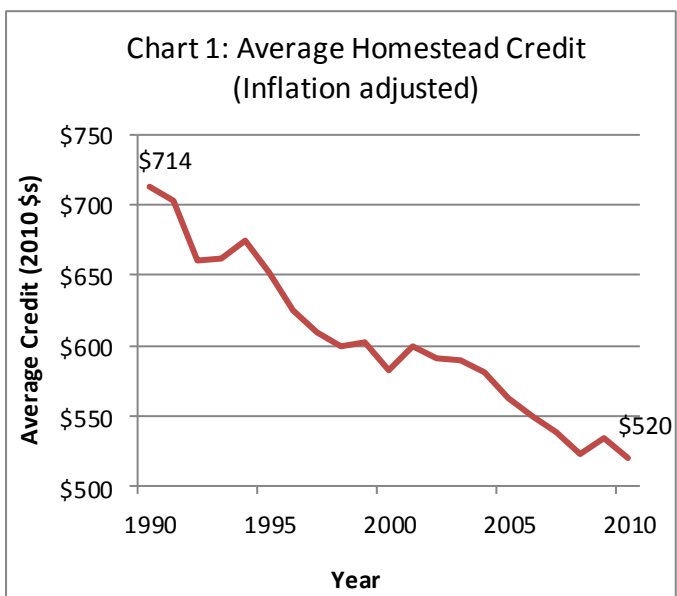
One way of measuring the decline of the credit's value is to consider the average credit amount. In

1990, the average credit (in 2010 dollars) was \$714. By 2010, that amount had dropped to \$520, a decrease of 27 percent. Chart 1 shows the decline in the average Homestead Credit over the last 20 years.

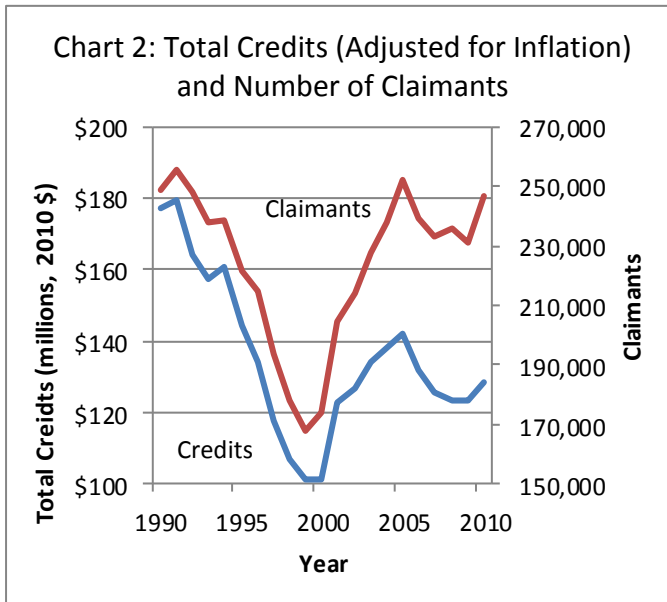
The average amount of the credit has been on a steady downward march since the early 1990s, but other trends regarding the Homestead Credit are mixed. The number of people claiming the credit the dropped precipitously between 1990 and 2000, by 30 percent, and has rebounded since then, as shown in Chart 2.

The increase in the number of claimants since 2000 is generally attributed to greater outreach efforts on the part of the Department of Revenue and increased electronic filing of taxes, which prompts filers to apply for the credit.

The real value of the total credits claimed also saw a sharp decline between 1990 and 2000, with the total credit amount down by more than 40 percent over



those ten years. Since 2000, total credits have increased somewhat, but in 2010 the total credit amount is 27 percent below the level in 1990.



### Formula Factors Are Infrequently Updated

Much of the decrease in the value of the Homestead Credit is because the state has not adjusted the credit to take inflation into account. The state uses several factors to calculate an individual’s Homestead Credit. For filers with income below a certain threshold (\$8,060 in 2010), the credit is 80% of their property taxes, up to the maximum benefit amount. For filers above the income threshold, the credit is calculated in a way that results in a smaller benefit.

Prior to 2010, the Legislature rarely made changes to the factors used to calculate the Homestead Credit. As shown in Table 1, the most recent adjustment to

Factor	Last Increase Prior to 2010
Income threshold at which maximum credit is received	1990
Maximum benefit amount	1991
Maximum property tax subject to credit	1991
Maximum income to receive any credit	2000

the formula was made in 2000, when the Legislature increased the maximum income at which filers were eligible to receive any credit. Other formula factors have not been updated since the early 1990s. Here is how the real (inflation-adjusted) value of the formula factors has changed between 1990 and 2010:

- The income threshold for the maximum credit has decreased from \$13,347 to \$8,060, or 40 percent;
- The maximum credit amount has decreased from \$1,802 to \$1,168, or 35 percent;
- The maximum property tax subject to the credit has decreased from \$2,252 to \$1,460, or 35 percent; and
- The maximum income to be eligible for any credit decreased from \$30,031 to \$24,680, or 18 percent.

### Inflation and the Recession: A One-Two Punch

One effect of the national recession is that incomes are down. With lower incomes, more people are eligible for the credit, even taking into account the extent to which the upper income limit has eroded over the years due to inflation.

The increase in the number of people claiming the credit has not kept pace with the increase in the total value of the credits. In 2010, the number of people claiming the Homestead Credit increased by nearly 16,000, a 6.9 percent increase over 2009.

This jump brought the number of people claiming the credit to 247,000, which is similar to the number of people claiming the credit in 1992. But that year, the total value of the credit in 2010 dollars was \$164.0 million, 28 percent higher than the \$128.5 million in credits claimed in 2010.

The Homestead Tax Credit provides much less property tax relief than it once did because it has been severely eroded by inflation. A repeal of the automatic adjustments for inflation, which were added in the 2009-11 budget, would decrease the amount of money available for property tax relief, and increase property taxes paid by low-income owners and renters.

Tamarine Cornelius, May 2011