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7% HOMESTEAD CAP SHOULD BE RENEWED

New, More Comprehensive Civic Federation Analysis Shows Benefits Outweigh Costs

CHICAGO – The Civic Federation announced Monday that it would maintain its support for extending the Alternative General Homestead Exemption (also known as the "7% cap") for another three years. The position is based on a new Federation review of the over 1.7 million Cook County properties affected by the cap, in which the potential effects of eliminating, extending, or expanding the exemption are analyzed.

The purpose of the homestead exemption is to mitigate the impact of rapid appreciation in the residential real estate market and the resulting higher property taxes on rapidly-appreciating owner-occupied homes. Although it is **not a replacement for comprehensive property tax reform**, the Federation found that the "7% cap" has contributed to residential stability in the Cook County property tax system by both limiting and smoothing annual increases in the taxable value of homestead properties. "The Civic Federation believes that the benefits of the Alternative General Homestead Exemption outweigh its costs in terms of the portion of the tax burden shifted to non-homestead and slowly-appreciating homestead properties," said Laurence Msall, president of the Civic Federation. "However, it is also important that public officials and taxpayers recognize that property valuation is not the only element affecting property taxes. Local governments' demands for larger and larger property tax levies are the most significant contributor to higher property taxes."

Unlike other published reports, the Federation's analysis of the "7% cap" examines changes in tax bills as compared to the previous year and uses actual 2005 assessment data. According to the Civic Federation's latest estimates, eliminating the "7% cap" would create a median property tax increase of 36.4% over the previous year for Chicago homeowners in 2006, 24.3% for northwest suburban homeowners in 2007, and 10.9% for southwest suburban homeowners in 2008. In contrast, if the exemption were renewed at the current maximum of $20,000, the median tax increase over the previous year would be 10.6% in Chicago in 2006, 0.2% in the northwest suburbs in 2007, and median taxes in the southwest suburbs for homeowners would decline by -2.6% in 2008. The Federation does not support raising the maximum exemption level to $60,000 as proposed in Senate Bill 2691 because this would create too large of a tax burden shift.

The effects of the "7% cap" on non-homeowner properties vary by class of property. However, the Civic Federation has found that the average effect of an extension of the homestead exemption on most other classes of property including commercial properties is to **reduce their median property tax cut**. In other words, properties in those classes will pay a median of 5% more than if the exemption were eliminated, but they will still pay on average **less in property taxes than they did the previous year**. This occurs both because commercial properties in Cook County have been appreciating at a slower rate than residential properties and because the total taxable value of all properties grows faster than the local governments' tax levies, thus driving down tax rates. If the relative rise in a property's taxable value is less than the relative fall in the composite tax rate, the taxes owed by that property will decrease.

"The '7% cap' has effectively served as a shock absorber, blunting the effects of rapid appreciation in the real estate market and should be renewed for three years with an exemption limit of $20,000," said Msall. "All the same, the measure is a short-term fix, and if in 2009 the housing market has cooled and residential assessment increases have stabilized, the General Assembly should allow the exemption to sunset."

The Civic Federation is an independent, non-partisan government research organization founded in 1894. The Federation's membership includes business and professional leaders from a wide range of Chicago area corporations, professional service firms and institutions.

Civic Federation Position Statement
November 27, 2006

Alternative General Homestead Exemption Extension

Position

The Civic Federation has recently completed a new, comprehensive analysis of the Alternative General Homestead Exemption (also known as the "7% cap"). Unlike other published reports, this analysis examines changes in tax bills as compared to the previous year and uses actual 2005 data. The analysis focuses on the potential effects of eliminating the expanded exemption, extending it for an additional three years, or expanding the maximum amount of the exemption. Based upon the results of this analysis, **the Federation maintains its support for extending the exemption through tax years 2006-2008 at the current maximum exemption level of $20,000 in taxable value** (equalized assessed value). The Federation does not support increasing the maximum exemption level to $60,000 as proposed in Senate Bill 2691.

In January 2004, The Civic Federation gave qualified support to the original Alternative General Homestead Exemption based on our expectation that the Cook County Assessor would use the expanded exemption to increase transparency in the assessment process and provide a smoothing of property tax increases for homeowners over the course of the three-year assessment cycle. Although it is **not a replacement for comprehensive reform** of the property tax system, the "7% cap" has contributed residential stability to the Cook County property tax system by both limiting and smoothing annual increases in the taxable value of homestead properties. The "7% cap" has effectively served as a shock absorber, mitigating the effects of rapid appreciation in the residential real estate market on the taxable value and resultant taxes of rapidly appreciating owner-occupied homes. The Civic Federation believes that the benefits of the Alternative General Homestead Exemption outweigh its costs in terms of tax burden shifted to non-homestead properties and homestead properties that are appreciating slowly. But property valuation is only one element affecting property taxes. Of even greater significance is the demand that local governments, particularly school districts, place on property tax payers to fund their operating costs.

Data Analysis Summary

The Civic Federation has completed its evaluation of changes in property taxes owed for each of the 1.7 million parcels in Cook County from 2002-2008 with and without the "7% cap". Preliminary results are reported in the attached tables. The full report is being prepared for publication in January. Assessed values were provided by the Cook County Assessor's Office, and the majority of 2006 values reflect actual 2006 assessments for the City of Chicago.

According to the Civic Federation's latest estimates, eliminating the "7% cap" would create a median property tax increases of 36.4% over the previous year for Chicago homeowners in tax year 2006, 24.3% for Northwest suburban homeowners in 2007, and 10.9% for Southwest suburban homeowners in 2008.

If the exemption were renewed at the current maximum of $20,000, the median tax increase over the previous year would be 10.6% for Chicago homeowners in 2006 and 0.2% for Northwest suburban homeowners in 2007. Southwest suburban homeowners would realize a median tax decrease of -2.6% for in 2008. Finally, if the exemption were expanded to a maximum of $60,000 in EAV, the median tax decrease would be -3.4% for Chicago homeowners in 2006, -10.3% for Northwest suburban homeowners in 2007, and -2.6% for Southwest suburban homeowners in 2008.

Effects on non-homeowner properties vary by class. Class 2 properties that do not qualify for the homeowner exemption (e.g., rentals, second homes) will experience the largest tax increases in any scenario. This is because they have seen significant appreciation in their property values, as have homeowners, but they are not eligible for the homeowner exemption. In Chicago tax year 2006, non-homeowner Class 2 properties are expected to see a median tax increase of 18.9% if "the 7% cap" is extended at $20,000, 25.9% if it is expanded to $60,000, and 18.0% even if it is eliminated.

Many vacant (Class 1) properties have also been appreciating rapidly in recent years, and their taxes have also increased. Class 3 apartment buildings have seen declines in their taxable value due to Cook County ordinances reducing their assessment level from 33% of market value in 2002 to 20% of market value in 2008. It is worth noting that this reduction has created its own tax burden shift onto other classes of property. The property appreciation for non-profit, commercial, and industrial properties has generally been slower than that of residential properties, leading to tax cuts for many of those properties. <u>In 2006, commercial properties in Chicago are estimated to see a median tax cut of 4.0% even if "the 7% cap" is continued in its current form.</u>

If "the 7% cap" were eliminated, we estimate that non-homeowner properties in Chicago tax year 2006 would owe a median 5% less in property taxes than if it is continued in its current form. However, homeowners' taxes would be 16.0% higher if "the 7% cap" is not continued with a $20,000 maximum exemption. It is important to note that the effect of "the 7% cap" on Classes 3 through 9 in Chicago tax year 2006 is to *reduce their median property tax cut*. **In other words, properties in those classes will pay a median of 5% more than if "the 7% cap" were eliminated, but they will still pay on average *less* property taxes than they did the previous year.** This occurs because the total taxable value of all properties grows faster than the local governments' tax levies, thus driving down tax rates. If the relative rise in a property's taxable value is less than the relative fall in the composite tax rate, the taxes owed by that property will decrease. Similarly, properties whose taxable value has been frozen by the Senior Citizens Assessment Freeze Homestead Exemption see their property taxes decline each year that the composite tax rate declines. **The effect of "7%" on the vast majority of taxpayers with a "senior freeze" has been simply to reduce their property tax cut.**

There has been some discussion focusing on the potential negative impact of the Alternative General Homestead Exemption on the ability of school districts to access property value for taxation purposes. It has been suggested that the "7% cap" would cause certain school districts to reach their rate limits, particularly in their Education Fund, which provides funding for general operations. However, previous reports and this study have found that the

7% cap would only cause a few school districts that have limited property value to reach their rate limits. These few districts are identifiable by the fact that they are already levying at the maximum rate limit, and are confronted by a myriad of economic and fiscal problems that would be best addressed by providing targeted financial relief through the school aid formula or other mechanisms.

Given these projections, the Civic Federation believes that the Alternative General Homestead Exemption should be renewed for three years with an exemption limit of $20,000. Expanding the limit to $60,000 would shift too much of the tax burden onto non-homeowner properties and homeowner properties that are appreciating slowly. The “7% cap” mitigates the impact of rapid appreciation in the residential real estate market on homeowners whose properties are experiencing rapid appreciation. Once the housing market cools, the “7% cap” may will no longer be needed. **If residential assessment increases have stabilized by tax year 2009, “the 7% cap” should be allowed to sunset at that time.**

PRELIMINARY RESULTS

(Full Report forthcoming in January)

Median Projected Change in Taxes Owed *as Compared to the Previous Year* City of Chicago						
	2006					
	$			%		
Class	**7%**	**No 7%**	**$60k**	**7%**	**No 7%**	**$60k**
1--Vacant	$ 31	$ 11	$ 54	8.7%	3.2%	15.1%
2--Homeowner	**$ 255**	**$ 829**	**$ (69)**	**10.6%**	**36.4%**	**-3.4%**
2--Non-Homeowner	$ 483	$ 308	$ 680	18.9%	12.8%	25.9%
3--Apartment	$ (1,051)	$ (1,643)	$ (366)	-8.3%	-12.9%	-2.9%
4--Non-Profit	$ (377)	$ (692)	$ (12)	-5.7%	-10.5%	-0.2%
5a--Commercial	$ (216)	$ (488)	$ 94	-4.0%	-8.9%	1.6%
5b--Industrial	$ (517)	$ (734)	$ (266)	-10.8%	-15.4%	-5.6%
6-9--Incentives	$ (773)	$ (1,163)	$ (320)	-9.1%	-13.7%	-3.8%

Note: Results are for the 75.6% of properties that were the same class from 2002-2005. Exempt properties are excluded.

Median Projected Change in Taxes Owed *as Compared to the Previous Year* North Triad						
	2007					
	$			%		
Class	**7%**	**No 7%**	**$60k**	**7%**	**No 7%**	**$60k**
1--Vacant	$ (0)	$ 4	$ 12	-0.2%	8.1%	7.8%
2--Homeowner	**$ 0**	**$ 1,025**	**$ (396)**	**0.2%**	**24.3%**	**-10.3%**
2--Non-Homeowner	$ 47	$ 226	$ 418	2.6%	8.9%	11.7%
3--Apartment	$ (3,083)	$ (2,261)	$ (1,638)	-21.0%	-16.3%	-13.1%
4--Non-Profit	$ (1,502)	$ (669)	$ (649)	-19.8%	-14.2%	-9.6%
5a--Commercial	$ (2,385)	$ (1,054)	$ (759)	-12.6%	-7.7%	-5.3%
5b--Industrial	$ (3,409)	$ (1,192)	$ (1,439)	-11.8%	-4.4%	-7.0%
6-9--Incentives	$ (4,232)	$ (2,409)	$ (2,540)	-15.7%	-12.1%	-8.5%

Note: Results are for the 79.4% of properties that were the same class from 2002-2005. Exempt properties are excluded.

Explanatory Note: 2007 median tax changes are higher if the "7% cap" is eliminated than if it is continued because the change is relative to taxes paid in each scenario in 2006 (if the "7% cap" is ended for the City in 2006, the increase in EAV drops the rate for overlapping taxing bodies, reducing tax rates in the North and South for 2006).

Median Projected Change in Taxes Owed *as Compared to the Previous Year* South Triad						
	2008					
	$			%		
Class	**7%**	**No 7%**	**$60k**	**7%**	**No 7%**	**$60k**
1--Vacant	$ (7)	$ (65)	$ (0)	-1.3%	-9.7%	-0.1%
2--Homeowner	**$ (56)**	**$ 347**	**$ (73)**	**-2.6%**	**10.9%**	**-2.6%**
2--Non-Homeowner	$ 76	$ (102)	$ 157	3.5%	-5.0%	6.8%
3--Apartment	$ (660)	$ (1,448)	$ (303)	-7.7%	-15.6%	-4.2%
4--Non-Profit	$ (334)	$ (541)	$ (130)	-6.7%	-14.7%	-4.0%
5a--Commercial	$ 25	$ (661)	$ 246	1.0%	-7.5%	3.7%
5b--Industrial	$ (139)	$ (1,125)	$ 52	-1.2%	-9.3%	0.9%
6-9--Incentives	$ (482)	$ (1,317)	$ (215)	-3.4%	-10.6%	-2.3%

Note: Results are for the 81.3% of properties that were the same class from 2002-2005. Exempt properties are excluded.

Explanatory Note: Homeowner properties have a median tax cut of -2.6% whether the "7% cap" is maintained or expanded to a $60,000 maximum exemption because less than 2% of eligible properties would reach the $60,000 limit.

Major Assumptions

PIN-level Assumptions

1. Class 3 assessment levels drop from 26% in 2005 to 24%, 22%, and 20%, in 2006-2008, respectively (per County ordinance)
2. Multipliers (projections provided by Cook County Assessor's Office): 2006 = 2.72, 2007 = 2.83, 2008 = 2.95
3. Assessed Value projections provided by Cook County Assessor's Office (includes actual AVs for Chicago Triad for those that have already been determined)
4. Projections are only for those properties that existed in 2005. No new PINs are created, but new property amounts are included for the purposes of tax rate calculation.
5. Each property remains in the same class as it was in 2005.
6. No property sales are assumed (a homestead sale would reset the homeowner exemption at $5,000).
7. TIF increments are calculated for each PIN in each scenario and aggregated to the tax code level, where any negative increments are changed to zero.
8. Co-ops are treated as normal homeowner properties because their homeowner exemptions cannot be reliably replicated.

Tax Rate Assumptions

1. New property in Cook County and other counties is assumed to increase by the average increase of the last three years (2003-2005).
2. EAV in other counties is assumed to increase by the average increase of the last three years (2003-2005).
3. Cook County railroad, air pollution, and use tax EAV amounts are assumed to increase by the average increase of the last three years (2003-2005).
4. There are no disconnected TIFs, annexations, or disconnections in any county.
5. Tax levies are assumed to increase by the average increase of the last three years (2003-2005).
6. Percent burden in Cook County remains the same as it was in 2005 for taxing bodies that overlap other counties.
7. CPI projections used for Property Tax Extension Limitation Law (PTELL) computations are as follows: 2006 = 3.4% (from Cook County Clerk's 2005 Tax Rates press release), 2007 = 3.3% and 2008 = 2.5% (from Congressional Budget Office projections, www.cbo.gov).
8. Prior year aggregate extensions (for PTELL) are computed each year and carried forward.
9. Prior year Cook County EAV is computed each year and carried forward.