

FOCUS

18 June 2008 • No. 12

In brief

Whether it be taxpayers, reporters, or local officials, understanding of property assessments and their impact, if any, on property tax bills is often limited. This vignette involving a village's only two residents attempts to reduce the widespread confusion by offering some simple principles to remember.

Capitol notes

■ New May figures from the U.S. Senate Joint Economic Committee show that unemployment nationally rose from 5.0% in April to 5.5% and that nonfarm payrolls declined for the fifth consecutive month. However, first-quarter GDP growth was revised upward from 0.6% to 0.9%.

■ Meanwhile, in its quarterly economic outlook, the state's Department of Revenue projects state nonfarm employment to drop 0.4% in 2008 and remain stagnant in 2009. Corresponding national figures show 0.1% and 0.2% increases this year and next.

■ A Milwaukee County advisory panel has recommended that most parks funding be shifted from property to sales taxes. Whether lasting property tax relief would result was not said.

■ Former UW-Madison chancellor and Clinton cabinet member Donna Shalala is one of six individuals to receive this year's Medal of Freedom from President George W. Bush.

TO CITY COUNCIL
FOR YOUR INFORMATION *sd*

The most confusing tax issue of all

This is the time of year when property taxpayers often receive assessment notices, boards of review frequently meet, and confusion abounds. WISTAX revisits this murky issue.

Hands-down, one tax issue confounds citizens more than any other. Few people, including many in the media and government, correctly understand the relationship between property assessments and taxes.

A common misconception is that an assessment increase means a property tax increase—or that, alternately, during a market downturn, a reduced assessment means a tax cut. Given the widespread confusion, it cannot be said often enough: A rising (or falling) assessment does not necessarily mean higher (or lower) property taxes.

Value share, tax share

Unfortunately, this reminder leaves the taxpayer unsure of how to interpret an assessment change. Perhaps eavesdropping on a conversation in Littleton will help. Clarice and Dumford, the tiny village's only residents, recently received new assessment notices . . .

Clarice: G'morning, Dumford, did you get your assessment notice in the mail yesterday? Mine doubled—from \$100,000 to \$200,000.

Dumford: Yeah, it came. My assessment doubled, too. I don't know what I'll do when my property taxes double. I'm already paying \$1,000.

C: Dumfie, don't worry. Your taxes are not going up one cent.

D: You've got to be kidding. My assessment skyrocketed. Surely, my taxes are going to go through the roof.

C: No, dear. The village is not increasing its tax levy for the coming

year. Littleton's only expense is street plowing and maintenance, and those costs have remained the same.

D: Yes, Clarie, but . . .

Seeing the confusion on her neighbor's face, Clarice interrupted.

C: Dear, think about Littleton. It has only two properties, yours and mine. Last year, both were assessed at \$100,000.

D: So, \$100,000 for my house and \$100,000 for yours adds up to \$200,000 for the village.

C: That's right. I own half the town's value and so do you. Now, you said your property taxes were \$1,000, right? That means the village's total property tax collections last year were \$2,000. I paid \$1,000, and you paid \$1,000.

D: Oh . . . I own half of Littleton's total property value, and I paid half the taxes. Does it work like that everywhere, Clarie?

C: Yep. No matter how many properties a community has, no matter what its total property value. You pay the same share of a municipality's tax levy as your share of its property value.

D: But, Clarie, my assessment has doubled. What will happen to my taxes?

C: Dumfie, dear. Our houses and yards are identical. My assessment doubled, too. Both our properties would now sell for \$200,000.

Littleton's total value is now \$400,000—\$200,000 for me and \$200,000 for you. My property is half of the village's value, and so is yours. Nothing's changed.

D: So, I'll pay half the property taxes . . . like before?

C: That's right. And since the village still needs only \$2,000 in taxes, I'll pay half—\$1,000—and you'll pay half—\$1,000.

Budget up, taxes up

D: So, even though our assessments doubled, our tax bills won't change. But . . . what happens if the village starts garbage pick up? There's been talk, you know. That would cost Littleton another \$1,000.

C: Then both our tax bills would go up. They'd increase because village spending and taxes increased.

The village levy would grow to \$3,000—\$2,000 for streets and \$1,000 for trash pick up. We'd both have to pay \$1,500 in taxes. Half the property value, half the taxes, right?

D: Right! Property taxes would increase for budgetary reasons—and not because our assessments grew.

Different shares . . . and taxes

D: Clarie, did I tell you my sister's husband died? She's thinking of moving into town and staying with me. The problem is that I would have to add another bedroom and bath. A contractor tells me it would cost \$100,000.

C: Well, that *would* increase your taxes. Your assessment would jump from \$200,000 to \$300,000.

D: But my taxes didn't increase when my assessment rose from \$100,000 to \$200,000.

C: That's different. My assessment would be \$200,000 but yours would be \$300,000. You would no longer own half of Littleton's property value. The village's value would be \$500,000—\$200,000 for me and \$300,000 for you. Your property would account for 60% of the village's total property value.

D: So, if the village tax levy stayed at \$2,000, I'd have to pay \$1,200, rather than \$1,000?

C: Yes, dear—60% of the village's value, 60% of the taxes.

D: But what about your taxes?

C: Because my \$200,000 property would account for only 40% of Littleton's value, I'd pay 40% of the taxes, or \$800. You know, \$200,000 divided by \$500,000 is 40%.

Values down, taxes down?

Dumford admired the flowers that separated his yard from his neighbor's. Then, he turned to Clarice.

D: Clarie, I was talking to my cousin, the real estate agent. She said

that, with the weak housing market, homes are not selling and home prices could drop as much as 50%. Wouldn't that be good news? Lower assessments, lower property taxes, right?

D: Dumfie, dear. Then we'd only get \$100,000 if we sold our homes. Besides, our tax bills wouldn't change at all. We'd each own half the village's value—\$100,000 of the \$200,000 total. We'd each have to pay half the taxes—\$1,000, just as before.

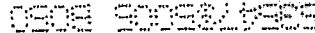
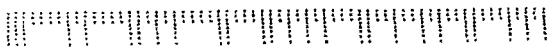
Rule of thumb

D: My brother lives in Bigville, where they just reassessed all properties. He told me yesterday that his assessment jumped 15%. Clarie, what should I tell him about his taxes?

C: Ask him how much the total assessed value of Bigville changed. If the city *doesn't* increase its tax levy, there are three possibilities.

First, if the city's assessed-value increase was more than your brother's 15% increase, his taxes would fall because his home's share of total city values would fall. Second, if Bigville's values increased 15%, his share of both valuation and taxes would remain unchanged. Finally, if city values rose less than 15%, his taxes would be higher. His home would be a larger share of the city's valuation. Larger share of value, large share of taxes, right?

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Focus

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brief

December property tax bills are just around the corner. Assessment increases often lead taxpayers to expect a tax increase. Official talk of tax rate cuts often leads citizens to expect lower tax bills. Neither expectation is necessarily correct. Taxpayers need to focus on what matters most: proposed budgets and tax levies.

Capitol notes

■ Rasmussen Reports released tracking poll results throughout 2006. A common story in Midwest industrial states was early difficulty for Democratic candidates followed by comfortable leads: Illinois (-6 pts. in April, now +8); Michigan (-5 in July, now +11); Ohio (+4 in Jan., now +12); Pennsylvania (-3 in April, +18 now).

Wisconsin is different. For much of the year, the Democratic lead has varied little—between four and eight points. Latest October results showed no change (+4). In Minnesota and Iowa, party candidates have traded leads several times.

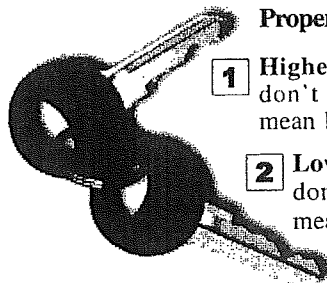
■ Riddled with small deductions and exemptions that few taxpayers use, Wisconsin's income tax is unnecessarily complex. Finding the same on the federal level, Oregon Senator Ron Wyden (D) urges a bipartisan reform effort, such as the successful Reagan-Bradley package of 1986.

Two keys to property tax understanding

PROPERTY COUNCIL
FOR YOUR INFORMATION

Focus has not recently discussed assessment. Responding to requests, we return to the topic. Still misunderstood, tax rates are also covered.

Local governments are busy setting property tax levies for the coming year. December tax bills can't be far behind. With them invariably comes surprise, relief, or anger. Two of the most common causes are confusion over assessment and confusion over tax rates.



Property Tax Keys

- 1 Higher assessments don't necessarily mean higher taxes.
- 2 Lower tax rates don't necessarily mean lower taxes.

Many property taxpayers typically and incorrectly believe that: (1) an increased assessment means a tax increase; and (2) official promise of a reduced tax rate means a tax cut. Neither is necessarily true.

Detour: Values confuse issue

Much of the confusion about assessment and tax rates has to do with a third factor: property values. If values never change, assessments would never have adverse tax consequences . . . and tax rates would rise and fall with state and local budget decisions.

Of course, property values do change. The market for most types of property in most parts of the state has, until recently, been strong. Since 2000, the total value of Wisconsin residential property has increased an average of almost 10% annually.

Such rapid growth allows public officials to tout falling tax rates, even if they are raising taxes. And it means that assessments increase from time to time. Back to the confusion both cause.

Higher assessments

If explained in the usual way drawing on technical tax terms, an assessment increase can be daunting. However, understanding one important concept helps: A community's total tax levy is divided among individual properties according to each owner's share of total community property value.

Thus, if you own 1% of a community's total value, you pay that same 1% of total property taxes. Suppose your home and lot are assessed at \$200,000 and the total value of your community is \$200 million (m). Further suppose that the community's total property tax levy is \$2m. You own 0.1% of the community's value, so you are responsible for 0.1% of the levy, or \$2,000 (\$200m X 0.1%).

Does a rising assessment guarantee a tax increase? Not at all. What matters is not the dollar value of the assessment but your share of total community valuation *relative* to other taxpayers. Consider a few simple examples in a town with only two properties, each valued at \$100,000, and a town tax of \$4,000.

First case. In the first scenario just outlined, each of the two homeowners accounts for one-half of town value (\$100,000/\$200,000 = 1/2). So each will pay one-half of town taxes, or \$2,000 (1/2 of \$4,000 = \$2,000).

Second case. Now, assume the town's assessments are updated and each home is now worth \$200,000. One owner immediately begins to worry about his \$2,000 tax bill doubling. But will it? Each owner still accounts for one-half of the town's value (\$200,000/\$400,000), and each still pays one-half of the taxes (\$4,000 X 1/2 = \$2,000) that the town levies.

Finding the Tax Rate

$$\text{Tax Rate} = \frac{\text{Tax Levy}}{\text{Property Valuation}} = \frac{\$4,000}{\$200,000} = .02^*$$

* Or \$20 of property tax for every \$1,000 of property value.

The assessments doubled, but the tax bills remained the same. Why? First, each owner's home value increased at the same rate (100%), and each still owned the same share of the town's total value. And, second, the \$4,000 town levy did not change.

Third case: More spending. What if the levy did change? Suppose the town asks for 50% more taxes, or \$6,000. Even though each owner's share of town value remains one-half, each must now pay half of \$6,000, or \$3,000. Note that the tax increase is not due to the assessment change but, rather, to the town's tax increase.

Fourth case: Assessment change. The cause of tax increases is often growth in budgets and tax levies. However, there are times when an assessment change can mean a higher or lower property tax.

The following example illustrates how changing assessments can lead to higher taxes for some and lower taxes for others. The owners of the two \$100,000 homes again receive assessment increases, but this time the increases differ. One owner's valuation doubles, as before, to \$200,000. But the other's triples, soaring to \$300,000. The town's total value is now \$500,000, but one individual owns two-fifths (\$200,000/\$500,000) of the town's total value and the other owns three-fifths (\$300,000/\$500,000).

The result is bad and good news. Even if the town levy stays at \$4,000, the second owner faces a tax increase. With 60% of the town's value, he must pay 60% of the taxes (60% X \$4,000), or \$2,400. The first owner, however, receives some good news. Even though his home's value doubled to \$200,000, his share of town value fell from 50% to 40%. So his tax bill drops to \$1,600 (40% X \$4,000). Clearly, there are cases when higher assessments result in tax increases and decreases.

Lower tax rates

Just as rising property values can lead to taxpayer anxiety over rising assessments, they can also be used to mask local tax increases. Imagine a mayor who proudly announces a 5% drop in the tax rate. Many residents take this news at face value and eagerly await a 5% drop in their tax bills. Should they? Not if they understand what a tax rate is.

The idea is fairly straightforward, as the picture above suggests. Take the total tax levy and divide by the community's total property value; the

result is the tax rate. Thus, if the town wants to collect \$4,000 in taxes and its total value is \$200,000, then the tax rate is: \$4,000 (tax levy) / \$200,000 (total town value), or .02 (see figure, left).

Sometimes, the tax rate is given as a mill rate, or the amount of taxes due for each \$1,000 of property value. In this case, the levy per \$1,000 is: \$4,000 / \$200 (thousand), or \$20 for every \$1,000 of value. Whether the rate is .02 or is \$20 per \$1,000, the tax bill is the same (\$2,000).

Because property values have been increasing, it has been easy in recent years for local officials to point to stable or falling tax rates, even when taxes are rising. Returning to the prior town example, suppose total property values jump 50%, from \$200,000 to \$300,000. As long as the town board increases taxes less than 50%, the tax rate drops.

For example, if the levy is raised \$500, or 12.5%, to \$4,500, the tax rate will still drop from .020 (or \$20 per \$1,000) to .015 (or \$15 per \$1,000). The math behind the new tax rate is: \$4,500 / \$300,000 = .015.

Final word

Unhappy taxpayers need to focus on local budgets and tax levies. Remember the two keys (see opposite side): Higher assessments and lower tax rates don't guarantee lower taxes.

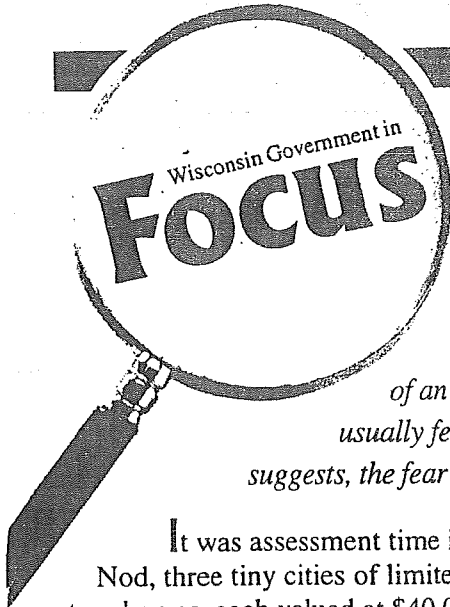
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Reassessment—a tale of three cities

▶ When taxpayers learn of an assessment increase, they usually fear a tax hike. As this tale suggests, the fear may be unfounded.

It was assessment time in Winken, Blinken and Nod, three tiny cities of limited means. Each had only two homes, each valued at \$40,000. Assessment news travelled fast, and even small increases caused concern.

Winken: Assessments Rise; Taxes Don't

In Winken, where assessments had more than doubled, the reaction of one woman was typical: "What will I do? My assessment went up 150%. They say my \$40,000 house is now worth \$100,000. I can't afford a 150% tax increase!"

"Balderdash," bellowed a deep voice. "Your taxes won't change a dime." A small, stout gnome appeared from behind a stump. He began to draw as he explained:

"Winken only has two houses, each assessed at \$40,000. The city's total assessed value is \$80,000.



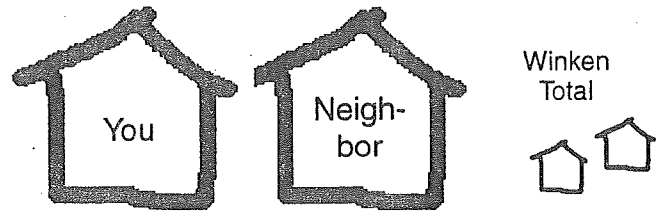
Asmnt.	\$40,000	+	\$40,000	=	\$80,000
	50%		50%		100%

"Last year, total property taxes levied—or charged—in Winken were \$4,000. Your home was half (\$40,000/\$80,000) the city's assessed value. So you paid half the taxes, or \$2,000. Your share of Winken's assessed value is your share of the total tax bill." The gnome wrote:

Taxes	\$2,000	+	\$2,000	=	\$4,000
	50%		50%		100%

"But our assessments jumped 150%. My house and my neighbor's are now valued at \$100,000. We're going to get killed when tax bills come out in December," she cried. A look of disbelief crossed the gnome's face. He hurriedly began to sketch and talk, only this time, the houses were bigger . . .

"Your house is assessed at \$100,000, just like your neighbor's. Winken's total assessed value is now \$200,000. Your assessment went up 150%; your neighbor's went up 150%; Winken's total rose 150%.



Asmnt.	\$100,000	+	\$100,000	=	\$200,000
	50%		50%		100%

"Your home is *still* half (\$100,000/\$200,000) of the city's assessed value. You're *still* going to pay half the taxes. The tax levy, the property taxes to be collected, isn't changing; so you'll *still* pay \$2,000—or half of \$4,000." He scribbled on his blackboard:

Taxes	\$2,000	+	\$2,000	=	\$4,000
	50%		50%		100%

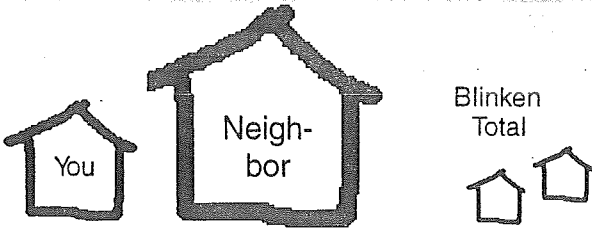
The Winken woman looked relieved. "You mean my taxes will stay the same, even though my assessment rose 150%?" "That's right," said the gnome. "The only way your property taxes will rise is if local governments increase their budgets and seek to collect more taxes through their levies."

Blinken: Assessments Rise; Taxes Rise and Fall

The Winken woman's uncle was visiting from sister-city Blinken. Things were much the same there: two homes each valued at \$40,000, each responsible for \$2,000, or half the \$4,000 in total property taxes.

When the gnome asked what had happened to assessments in Blinken, the uncle told him his valuation had doubled to \$80,000, and his neighbor's \$40,000 home was now assessed at \$120,000. "My taxes are going to jump for sure," the uncle exclaimed. The gnome began to talk:

"Like Winken, Blinken's total assessed value grew from \$80,000 to \$200,000, a 150% increase. Your assessment doubled to \$80,000, and your neighbor's tripled to \$120,000.



Asmnt. \$80,000 + \$120,000 = \$200,000
 40% 60% 100%

“But now your house is only 40% of the total assessed value—\$80,000/\$200,000 is 40%. So, your share of Blinken’s total value has dropped from 50% to 40%. Your taxes will drop from 50% to 40% of the total.”

Taxes \$1,600 + \$2,400 = \$4,000
 40% 60% 100%

The Blinken uncle couldn’t believe it—his assessment had doubled and his taxes were falling. The gnome explained, “If the tax levy stays at \$4,000, your December tax bill will be \$1,600. Your assessment is 40% of Blinken’s value; you pay 40% of the taxes.”

“Do my neighbor’s taxes go down, too?” inquired the uncle. “Nope,” said the gnome. “His home is no longer half of Blinken’s assessed value; it’s now 60%. So, he will have to pay 60% of the levy, or \$2,400 in taxes.”

Nod: Spending Affects Taxes

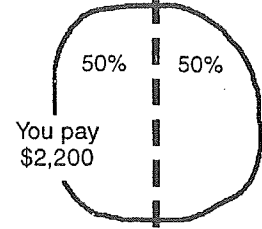
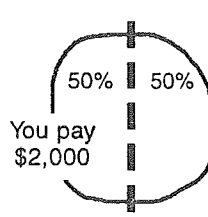
Cousin Naomi breathed a sigh of relief from the other room. Because there had been no assessment change in Nod, she said she was safe from a tax increase. Both homes there were worth \$40,000, and a weak real estate market had left home prices flat.

The all-knowing gnome couldn’t believe his ears. He quickly drew two circles and started chattering again . . .

“Your home and your neighbor’s are both assessed at \$40,000. No change. You each represent half of Nod’s value; you each pay half the tax levy, whatever it is.

Last Year’s Tax
 Levy = \$4,000

This Year’s Tax
 Levy = \$4,400



“Last year, when total taxes were \$4,000, you each paid half—\$2,000. This December, the tax levy is to rise 10% from \$4,000 to \$4,400. You’ll still pay half—half of \$4,400, or \$2,200.”

Cousin Naomi from Nod looked confused. So, the gnome continued: “Assessments don’t affect how much is going to be *taxed*; budgets determine that. Assessments only affect how the tax bill is *divided* among the property owners, once the tax levy is set.”

The Moral of the Story

When assessments rise, tax rates usually drop. But taxpayers don’t need to understand tax rate math to know that when assessments change, they should compare their percent rate of increase with the average community increase.

If the change is greater than the average, a tax increase is possible; the owner’s property now represents a larger share of total valuation. If the change is the same or less than the average, a tax increase is possible when the total property tax levy is increased. A smaller-than-average assessment increase could even mean a tax cut!

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