Fiscal Note & Local Impact Statement

123 rd General Assembly of Ohio

BILL:	**Sub. S.B. 6 (with amendment 0672)**	DATE:	**April 14, 1999**
STATUS:	**In House Ways and Means – Subcommittee on Homestead Exemptions**	SPONSOR:	**Sen. Armbruster**

LOCAL IMPACT STATEMENT REQUIRED: **No — No local cost**

CONTENTS: **Increase qualifying income limit for the homestead exemption and index all qualifying income brackets to inflation using the GDP deflator.**

State Fiscal Highlights

STATE FUND	FY 1999	FY 2000	FUTURE YEARS
General Revenue Fund			
Revenues	- 0 -	- 0 -	- 0 -
Expenditures	$9.5 million - $13.5 million	$10.35 million to $14.35 million	$11.20 million to $15.20 million annual increase

Note: The state fiscal year is July 1 through June 30. For example, FY 2000 is July 1, 1999 – June 30, 2000.

- The cost of future years will grow $850,000 each year, on top of the $9.5 million - $13.5 million initial increase in tax year 1999. Therefore, tax year 2000 will cost $10.35 million to $14.35 million, tax year 2001 will cost $11.20 million to $15.20 million, tax year 2002 will cost $12.05 million to $16.05 million, and so forth.

- The bill indexes qualifying income brackets to inflation using the gross domestic price deflator measurement.

Local Fiscal Highlights

- No direct fiscal effect on political subdivisions.

Detailed Fiscal Analysis

The homestead exemption program allows senior citizens, disabled persons, and surviving spouses who own and occupy their principal residence and whose total income is less than $20,800 to receive a reduction in taxable property value. The program cost is reimbursed by the state to local taxing districts. Sub. S.B. 6 would increase qualifying income brackets and index to inflation all three qualifying income brackets. To determine state cost of the bill, two components must be estimated: (1) Tax Year 1999 increase in new homestead participants from increasing the qualifying income brackets, and (2) Number of new homestead participants and participants changing brackets in future years from income brackets being indexed for inflation.

Discrete Increase in Maximum Qualifying Income Bracket

Using 1997 data (most recent data available) on the number of homestead applicants by current income brackets, LBO estimated the additional cost from a discrete increase in the qualifying income brackets.[1] Table 1 shows the current income brackets, Sub. S.B. 6 income brackets, and the estimated cost of Sub. S.B. 6 by brackets. Since exact data is not available on individual homesteader's income, observations from the 1995 total income bracket change were used to determine the movement of homesteaders in Sub. S.B. 6 brackets.[2] The next section contains the methodology of determining homesteader movements.

All the persons in the less than $10,800 income bracket would still qualify at the proposed less than $14,200 bracket. Assuming 68 percent of the qualifiers in the $10,800-$15,800 bracket would move into the proposed less than $14,200 tax bracket, the increased additional cost would be $4.0 million to $6.0 million. Using the same assumption, 32 percent of the persons in the $10,800-$15,800 bracket and 100 percent of the persons in the $15,800-$20,800 bracket would then qualify for the $14,200 -$20,800 income bracket, increasing the program cost by another $3.0 million-$5.0 million. If 38,000 new persons would now qualify due to the maximal income increase of $20,800 to $27,400, then an additional $2.5 million in increased cost is estimated. Therefore, tax year 1999 will see a $9.5 million to $13.5 million increase from raising the qualifying income brackets.

Table 1: Initial One Year Per Income Bracket Cost Increase of Sub. S.B. 6

Current Brackets	Sub SB 6 of 123rd G.A.	Estimated Cost Increase
T.I. ≤ $10,800	T.I. ≤ $14,200	$4.0 million to $6.0 million
$10,800 < T.I. ≤ $15,800	$14,200 < T.I. ≤ $20,800	$3.0 million to $5.0 million
$15,800 < T.I. ≤ $20,800	$20,800 < T.I. ≤ $27,400	$2.5 million
T.I. > $20,800	T.I. > $27,400	$0

[1] Department of Taxation data set.

[2] Since federal retirement benefits are not indexed to inflation and fixed at the level when first received, it must be the case that other sources of income cause homesteaders to move between brackets or enter/exit the program.

Inflationary Indexing of Qualifying Income Brackets

The qualifying income brackets proposed by Sub. S.B. 6 are effective in tax year 1999, which will become the base year in which the gross domestic price (GDP) deflator is applied.[3] LBO subscribes to two forecasting firms and data was used from one of these firms, WEFA, to index Sub. S.B. 6 qualifying income brackets to inflation through 2004. This is presented in Table 2. Taxable reduction values would not be changed.

Table 2: Inflationary Adjustment of Qualifying Income Brackets through 2004

$14,200 HEX Bracket		**$20,800 HEX Bracket**		**$27,400 HEX Bracket**	
Year	**Indexed Bracket**	**Year**	**Indexed Bracket**	**Year**	**Indexed Bracket**
1999	$14,200	1999	$20,800	1999	$27,400
2000	$14,500	2000	$21,300	2000	$28,000
2001	$14,900	2001	$21,700	2001	$28,600
2002	$15,200	2002	$22,200	2002	$29,200
2003	$15,500	2003	$22,700	2003	$29,800
2004	$15,800	2004	$23,100	2004	$30,400

Inflationary Indexing of Total Program Cost

The second component of the analysis is to estimate program cost in future years. Using the WEFA forecast of GDP deflator and assuming an increased cost of $11.5 million in the year 1999, it is possible to project future years' cost of the homestead exemption program This is graphically done in Figure 1. First, data from 1985 through 1997 is adjusted for inflation, using the GDP deflator measure, to Tax Year 1997 (most recent data). A solid, vertical line is drawn at tax year 1997 to indicate the actual (adjusted) data from projected data. Second, the income bracket increases of 1988 and 1995 are indicated with a solid, vertical line, along with the Sub. S.B. 6 tax year 1999 bracket increase.

Figure 1 data between 1997 and 1999 represent the projected trend under current law. From the base year of 1999, three projections are presented in Figure 1. The lowest line represents no change to the homestead exemption program Based on historical data, the state cost decreases by about one-percent each year as homesteaders' come in and out of the program due to changes in their total income. LBO projects that the homestead program will cost $63.1 million in the year 1999 under current law, *ceteris paribus*.

The middle project line represents a $11.5 million increase in the homestead program due to raising the qualifying income brackets and not adjusting the brackets for inflation. In year 1999, the homestead program would cost $74.6 million from just increasing the brackets.

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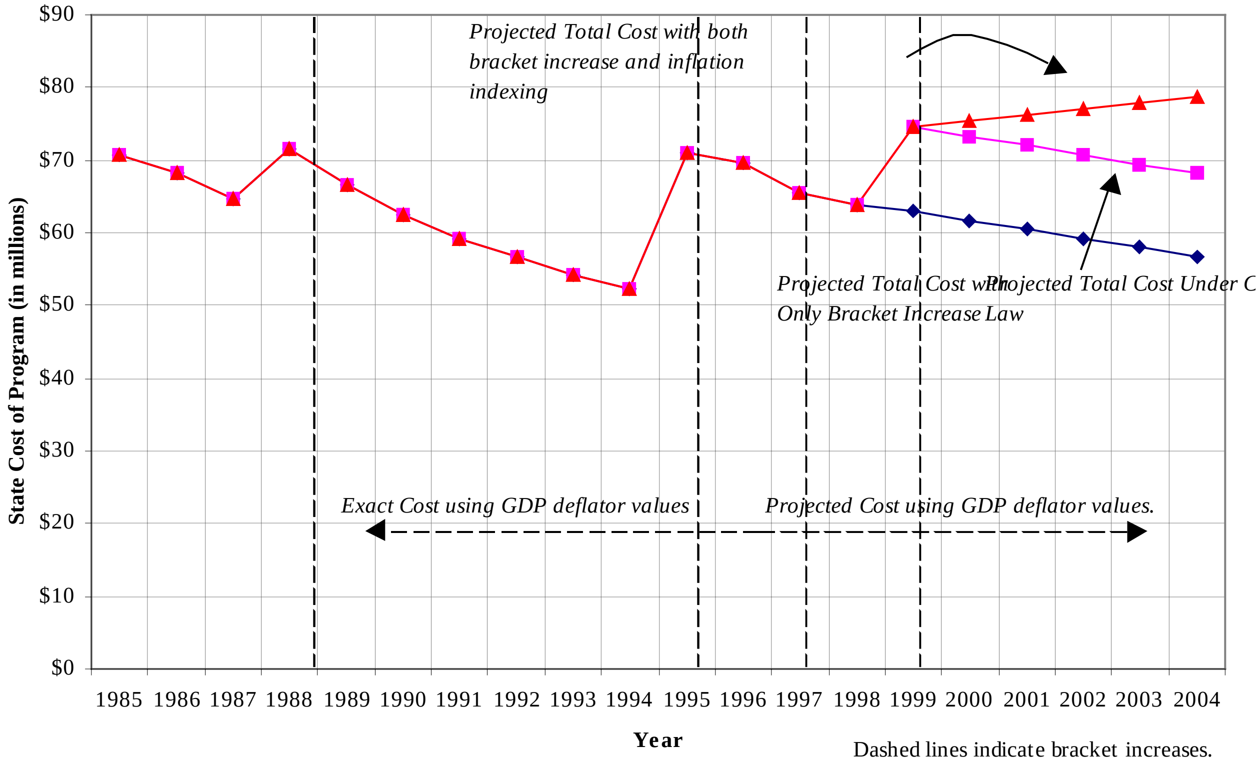
[3] The GDP deflator, as a measure of the overall price change in domestic goods, encompasses a broader range of domestic products than the consumer price index. It also allows for comprehensive substitution among goods and services.

The top projection represents Sub. S.B. 6. In tax year 1999, there will be a $11.5 million increase in the homestead program cost due to increasing the qualifying income brackets and an additional $850,000 each successive year from indexing the income brackets to inflation.[4] The difference between the top projection and the bottom project (current law) is the difference in annual cost, which grows by an additional $850,000 each year.

Figure 1: Projected Program Cost With and Without Brackets and/or Indexing



Conclusion

The total effect of indexing the homestead program to inflation and increasing the qualifying income brackets is to increase the program cost by $9.5 million to $13.5 million in the first year (1999) and $850,000 each successive year thereafter, which, in total, is a $10.35 million to $14.35 million increase for the second year with further increases each successive year.

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[4] WEFA forecasts an annual increase of 2.1% in the GDP deflator. Homestead exemption costs decreased by 1%-2% annually over the 1988-1995 period, with later decreases being about 1%. Therefore, indexing will work to increase program costs about 2% above where they would have been otherwise, resulting in a net increase of about 1% annually.