

To: Members, Income Based Education Tax Study Committee

From: Karen Horn, Director Public Policy & Advocacy

Date: December 21, 2022

Re: Draft Report Pursuant to 2022 Act 175, Section 5, Income-Based Education Tax Study Committee

The Vermont League of Cities and Towns supports legislation to reform Vermont’s tax system to ensure sustainability, affordability, equity, and balance. We support developing a transparent education finance system that reduces the education homestead property tax and more closely links voters’ actions in approving budgets to the taxes they pay to fund their school districts.

We have supported moving the homestead education tax to an income tax for several years. We believe this initiative would reduce the burden on Vermont property taxpayers overall, incorporate more uniformity in the net education tax paid as a percent of income, and, not incidentally, provide some opportunity for municipal voters to make long delayed investments in vital municipal services and infrastructure. As the committee is aware, in all but 25 of 247 cities and towns, the property tax is the only tax revenue source available to fund municipal expenditures.

Thank you for your efforts to develop a path forward that would move to an income-based homestead education tax in a timely and minimally disruptive manner should the legislature decide to proceed. We understand that there are many questions that need to be answered and that the transition to a new income based system for homestead taxes would need to be very carefully phased in, particularly if the transition is concurrent with the timeline for implementing new pupil weights.

Local officials believe it is imperative that the legislature address the endless increase in education costs and that it is every legislative committee’s responsibility to take on that work because virtually every committee’s work affects education in some respect.

The fundamental problem of escalating education costs is explained in the draft report Overview and Background section. “...unlike most funding structures, Vermont’s education expenditures are *not* a function of how much money is raised for education; instead, the converse is true: property tax rates to fund education are a function of education expenditures”.

While property tax rates in the Education Fund may have fluctuated over time, property tax dollars contributed to the Education Fund have increased every year except for FY23.

Education Property Taxes	
December 2022	
<i>Millions of Dollars</i>	
FY24 (projected)	\$1,295.6
FY 23 (projected)	1,198.1
FY 22	1,228.7
FY21	1,197.4
FY20	1,144.0
FY19	1,105.7
FY18	1,058.9

Joint Fiscal Office Education Fund Outlooks

In no less than eight places in the draft report, the mantra is repeated that each district’s education spending is determined at the local level, where school boards set budgets that must be approved by the voters. It tells only a piece of the story to repeat that school budgets are determined by school boards and local voters while leaving left unsaid that virtually every year the legislature also establishes new mandates and requirements for school performance, facilities, curriculums, services, supports and administration, that school boards must ensure are incorporated in the budgets presented to local voters. A cursory read of Title 16, reveals many of the requirements that have been embedded in statute over time.

In December 2018, there were 87,620.6 equalized pupils. Total Education Fund Uses equaled \$ 1,704.2 million. In December 2022, according to the consensus revenue forecast, there are 85,806 equalized pupils and that number is projected to decline to 84,890 in FY 24, the last year before new pupil weights begin to phase in. Total Education Fund Uses in FY23 are projected to be \$1,966.1 million, and in FY 24 as of this date Total Education Fund Uses are expected to increase to \$2,076.1 million. While obligations for adult education, community high school, renter rebate, reappraisal and listing are no longer included in the Education Fund, the normal cost of teachers’ pensions and other post-employment benefits (OPEB), special education, and universal school meals are now included as Education Fund obligations, as noted in the draft report.

According to the draft report and Tax Structure Commission, approximately 70 percent of homestead taxpayers pay some portion of their obligation based on income. In transitioning to a homestead education tax based entirely on income, we agree with the committee that for purposes of simplicity, Adjusted Gross Income should be used as the tax base for and education income tax and having the Department of Taxes administer the tax.

We do have a few preliminary questions regarding the draft report.

- What are the assumptions that lead to the recommendation to both maintain the current renter credit in current form and create a new nonrefundable credit for renters against the

education tax? We are confused by this section and imagine that members of the public will have similar questions.

➤Currently, the education property tax is the “flexible lever” to accommodate fluctuations in the Education Fund, or as we explain it, the education property tax is the backstop when other revenues fail to meet Education Fund obligations. If, as the draft report suggests, the non-resident property tax becomes the flexible lever, would only non-resident property taxpayers be the ones on the hook for increases when other revenues are insufficient to meet obligations? That is a significant burden on those taxpayers.

➤The report recommends allocating all education tax revenues to the Education Fund. Why would that not always be the case? It further recommends using education tax rates (homestead? Nonresident? Sales and use?) as flexible levers in case of underperformance or unexpectedly strong performance of education tax revenues. This recommendation seems to conflict with the reliance on the nonresident property tax payer noted in our comment above.

➤The committee recommends maintaining municipal involvement in the state property tax system. How would that work, especially for properties that would need to pay a homestead income tax and a nonresident property tax? How do the town and the Department of Taxes determine that the correct taxes were paid to each? How does the property owner stay on the right side of their property and income tax obligations? It seems that education taxes should all be paid to the same entity.

➤How would the new system more closely link voters’ actions in approving budgets to the taxes they pay to fund their school districts.

We hope that the legislature will consider moving the system for reappraising properties from the current unpredictable and unmanageable system that is based on falling below 85 percent or rising above 115 percent of the Common Level of Appraisal, to one that is on a predictable schedule. The Tax Department could establish a timeframe whereby every seven or so years a town would need to reappraise its properties. Towns would be grouped according to geographic areas, so that it would be easier to join together to hire appraisal firms. A version of a reappraisal schedule is used in many other states and provides predictability for the municipalities, the appraisal firms, the Tax Department and property owners. We are happy to talk more about this concept.

Your committee has done a tremendous amount of work to visualize necessary components of an income-based homestead education tax system. Yet there is far more discussion necessary and if such a system were put in place, we believe there would need to be at least a two-year period during which details of implementation were finalized before implementation was undertaken. As we noted above, it would be unhelpful to roll out this transition and the new pupil weighting system at the same time. In that circumstance it would be next to impossible to determine which new system was creating which problems or unintended consequences.

Thank you for the opportunity to testify.

VLCT Comment to the Tax Structure Commission, January 19, 2021

<https://lfo.vermont.gov/assets/Meetings/Tax-Structure-Commission/2021-01-25/ab39a2413f/VLCT-Comment-on-Draft-TSC-Report-1-19-2021.pdf>