

Recommendations to the Tax Panel

Susan Merrow

Co-Chair, 1000 Friends of Connecticut

Property Tax Working Group

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The Case for Property Tax Relief

In Connecticut, property taxes have been essentially the only source of revenue for municipalities. But although property taxes are relatively stable, they are highly regressive, and both horizontally and vertically inequitable.¹

- In Connecticut, the ninety percent of taxpayers with the lowest incomes pay two to seven times higher effective property tax rates – property taxes as a percentage of income – than the ten percent of taxpayers with the highest incomes.²
- For non-elderly households, property taxes as a share of family income for the bottom 95% are two to four times higher than for taxpayers in the top 5%.³
- Because the fair market value of residential property is sometimes not commensurate with the current income of residents (both renters and owners), persons with limited ability to pay are often charged property taxes they cannot afford.
- Owners of property having the same fair market value pay vastly different property taxes based on the town in which they live.
- Taxpayers in different towns receive very different levels of public services for the same amount of taxes paid.
- Great differences in property-tax based funding for public schools produce vast educational inequities between children in richer and poorer towns. Few municipalities are able to fully compensate for the state's inadequate fiscal support of the public schools – which the state is constitutionally responsible for maintaining.

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In general, see “Connecticut Property Taxes 2015: Time for a Change,” A Project of 1000 Friends of Connecticut, The Property Tax Work Group, April 2015.

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DRS Tax Incidence Study, December 2014, p. 21. In Connecticut, the DRS Study reports, the Suits Index, a measure of progressivity, is -0.39 for property taxes.(p. 15)

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Institution on Taxation and Economic Policy, Who Pays?, January 2015, pp.41-42.

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- Disparities among towns affect locational decisions, dis-incentivizing investment in places that would otherwise be attractive.

Are Local Taxes An Answer?

One way to reduce the reliance on local property taxes is to authorize municipalities to levy local-option sales or income taxes on taxpayers within their jurisdictions. But such local-option taxes would be subject to the same kind of horizontal inequities as property taxes, because “revenue capacity from new local-option taxes is not evenly distributed across municipalities.” As an analyst for the New England Public Policy Center put it,

Local-option taxes are likely to exacerbate fiscal disparities, because municipalities with low existing revenue-raising capacity often lack the tax bases for new local-option taxes.⁴

Accordingly, authorizing local-option taxes on sales and income should be rejected.

Instead, the Tax Panel should recommend the continuation of the policy adopted by the General Assembly in 2015: intercepting a portion of the state sales tax revenue before it is appropriated for state expenditures, and distributing it to municipalities in ways that diminish the disparate revenue-raising capacity of towns which currently exists because towns mainly depend on local property taxes to fund both educational and non-educational expenses.

The General Assembly in 2015 adopted an innovative mechanism for providing property tax relief to municipalities in the state: intercepting part of the state sales tax revenue before it was appropriated, and then directing it to be used to reduce the disparity in the ability of towns to raise revenue locally. In 2015, ½ of a percentage point (equal to about 7.9% of total sales tax revenue) of the sales tax was designated to be used in this fashion⁵:

- 1) part was used to reduce the disparity in the property tax on motor vehicles,⁶
- 2) part was used to direct additional PILOTs to municipalities with high shares of tax-exempt state property and college and non-profit hospital property,⁷ and
- 3) part was allocated to provide individually-identified grants to towns.⁸

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Bo Zhao, “The Fiscal Impact of Potential Local-Option Taxes in Massachusetts,” New England Public Policy Center, Working Paper 10-2 ((2010), p. 1.
<https://www.bostonfed.org/economic/neppc/wp/2010/neppcwp102.pdf>

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PA 15-244, Section 74, as modified by PA 15-5 (June Special Session), Section 132. This percentage would be used starting in 2018. In earlier years, a smaller percentage would be intercepted.

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PA 15-244, Sections 206-208, as modified by PA 15-5 (June Special Session, Section 494.

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PA 15-244, Sections 183-205.

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PA 15-244, Sections 207-208, as modified by PA 15-5 (June Special Session, Section 494.

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The first two allocations did in fact address disparities, but it is unclear if the third allocation does so. A tentative formula to distribute the third allocation after the first year was enacted, but the Office of Policy and Management was directed to make recommendations for improvement and enhancement of all of the provisions for distribution, including the formula for the third allocation.⁹

Recommendations

- The Tax Panel should recommend against authorization of local-option taxes on sales and income. (see above)
- The Tax Panel should recommend that that the state continue to intercept revenue for the purpose of rebalancing the overall tax structure in Connecticut by reducing the reliance on property taxes – and if necessary in future years, increase the amount of intercepted revenue in order to do so. The state should distribute those funds back to the towns in ways that reduce the gaps between objectively measured needs of each town and its capacity to raise revenue locally.
- The Tax Panel should recommend that the state continue to use part of the intercepted revenue for the purpose of reducing the disparity in the property tax on motor vehicles.
- The Tax Panel should recommend that the state continue to use part of the intercepted revenue to fully fund the PILOT for state property and the PILOT for college and non-profit hospital property used for educational and medical purposes. If the state is unable to fully fund these PILOTs, the state should continue to use the new formula established in PA 15-244 to provide as much aid as possible to those towns with higher percentages of state tax-exempt property.
- The Tax Panel should recommend that the General Assembly use the remaining or additional intercepted state revenue to eliminate the gap between the non-educational “need” of a municipality and its capacity to raise revenue to pay for its non-educational needs. A distribution formula which addresses closing this “need-capacity gap” – also known as the “cost-capacity gap” or the “municipal gap” – should be developed and implemented by the General Assembly.

The research on which the last recommendation is based was conducted by analysts of the New England Public Policy Center for the General Assembly’s Program Review and Investigations Committee.¹⁰ It is important to note that the NEPPC’s “measures of costs

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PA 15-244, Section 210.

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Bo Zhao and Jennifer Weiner, “Measuring Municipal Fiscal Disparities in Connecticut,” presented May 8, 2015. The report, the presentation, and appendix with supporting data are available at <https://www.bostonfed.org/economic/neppc/researchreports/2015/tr1501.htm>

and capacity, and therefore gap, do not represent actual spending or revenues, but instead are based on factors that are outside the control of local officials.”

Under this framework, a town that engages in wasteful spending would have higher actual expenditures but the same underlying costs as an otherwise identical town that is better managed. Likewise, two communities that have access to the same amount of economic resources have identical capacity, even if one chooses to levy a higher tax rate than the other.¹¹

This analysis removes from the computation of the need-capacity gap any tendency by town officials to game the system by increasing spending and/or increasing taxes. It excludes factors that can distort fair distribution, such as local decisions to pay employees a higher wage or to hire more employees, or to provide a higher than average level of services (on the cost side) or to raise or lower tax rates (on the capacity side.)

Instead, capacity is determined by the value of property in a town,¹² and municipal costs are computed based on five key factors outside the control of local officials:

- The unemployment rate
- Population density
- Private-sector wages
- Miles of locally maintained roads, and
- Jobs per capita in the town.¹³

Note that if state funds are distributed based on a “need-capacity gap” analysis, there is no reason to provide for a spending cap on increased local spending¹⁴ – since need is determined not by local officials, but by underlying objectively determined factors.

- The Tax Panel should recommend that if additional state assistance is required to ensure that the education provided in each town meets state constitutional standards of adequacy and equity,¹⁵ steps should be taken to intercept state revenues to provide funds to meet educational costs in an adequate and equitable manner, thus addressing what is necessary to provide a constitutionally sufficient education for each child. A distribution formula

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Zhao and Weiner, pp. 1-2.

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For a much fuller explanation, see Zhao and Weiner, pp. 2-5.

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For a much fuller explanation, see Zhao and Weiner, pp. 4-8.

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See PA 15-244, Section 207.

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See CCJEF v. Reil, (2010). Additional funding may also be necessary to provide adequate support for Educational Cost Sharing, to meet requirements of Horton v. Meskill, and to provide for an end to racial segregation, to meet requirements of Sheff v. O'Neill.

that closely reflects the real costs of educating students, including appropriate weightings for additional expenditures related to students with disabilities, English language learners and students from families living in poverty, should be constructed.

- The Tax Panel should recommend the institution of a reimbursable income-based circuit-breaker for both owners and renters, to provide relief to individual taxpayers who do not have the income necessary to pay property taxes even after they have been adjusted to reflect additional state funding directed to towns to reduce inter-town inequities.¹⁶ Because such a circuit-breaker does not do anything to close need-capacity gaps, however, it should complement, not replace, programs to reduce property tax disparities among towns.
- The Tax Panel should recommend investigation of other types of local revenue options, such as
 - Agreements for rental/lease of utility rights of way
 - Franchise fees for cable and internet providers
 - Greater shares of the real estate conveyance tax
 - Development impact fees
 - Increasing the state-determined valuations of state forest land (subject to PILOT)

16

See links to numerous analyses at <http://www.taxcreditsforworkingfamilies.org/state-resources/property-tax-circuit-breaker/>