



# CCM 2015 Testimony

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## *STATE TAX PANEL*

September 16, 2015

### TESTIMONY

of the

### CONNECTICUT CONFERENCE OF MUNICIPALITIES

The Connecticut Conference of Municipalities (CCM) represents over 95% of Connecticut's population. Thank you, on behalf of towns and cities across the state, for giving us this opportunity to speak to you about the State's tax structure and our ideas for improving the system for the benefit of taxpayers throughout Connecticut.

CCM urges you to consider that, while other factors have importance, quality of life issues are the most important factors businesses weigh in determining whether to relocate to or remain in a state. Factors such as quality schools, an educated workforce, safe neighborhoods, reasonable property taxes, and safe and reliable roads and bridges top the list of employers' "must haves". Further, all residents believe that laying the foundation for a world-class education, police and fire services and safe roads are core government services. No government service is placed above them. These are the services that towns and cities provide.

The future of Connecticut's citizens, depends on to a considerable degree on what you recommend -- and the actions taken by the General Assembly regarding those recommendations.

Overreliance on the property tax to finance local public services, particularly preK-12 public education, is the root cause of many of the public policy challenges facing Connecticut. You have the opportunity to recommend substantive changes to a dysfunctional property tax system, to catapult Connecticut back into the top of the list of states where businesses and residents strive to remain or relocate to.

The antiquated and inequitable property tax system continues to cause numerous problems, including the fiscal distress and decline not only of our cities, but also of our towns. It encourages the continued economic and racial segregation of our state. It often prevents municipalities from meeting the public service needs of their residents and businesses without levying a heavy local tax burden. It promotes bad land use decisions and contributes to costly and destructive sprawl.

In the last year, three events highlighted the problem with Connecticut's dysfunctional property tax system: (a) In March, US Secretary of Education, Arne Duncan, spoke of education disparities in the country and singled out over-reliance on the property tax for public education as a major culprit, (b) in December, the State Department of Revenue Services released a tax incidence study that confirmed the property tax is the most burdensome and regressive tax on Connecticut residents and businesses; and (c) the Federal Reserve Bank of Boston released a study of Connecticut's "fiscal disparities" that highlights how our property tax-only system of raising revenue for necessary local services contributes to fiscal stress.

### What Can Be Done?

CCM urges the Panel to consider the plight of businesses and residents and overhaul Connecticut's property tax system using proven approaches to release the property tax chokehold.

1. **Fully Fund PILOTs:** The State should increase and fully fund PILOT to provide reimbursement to municipalities for 100 percent of the revenue lost due to state-mandated property tax exemptions.
2. **Meet State Obligation to Fund Public Education:** Reforming preK-12 public education finance is a key to property tax reform in Connecticut. Chronic state underfunding of preK-12 public education is the single largest contributor to the overreliance on the property tax in our state. The ECS grant alone is underfunded by more than \$600 million. Special education costs are now approaching \$2 billion per year and impose staggering per-pupil cost burdens on host communities. *Special-education costs should be borne collectively by the State, not individual school districts.*
3. **Permit Municipal Local Revenue Diversification:** Connecticut is one of only 15 states that allows municipalities just the property tax. Plus, remember that most other states have county governments that levy taxes in addition to state and local taxes, and that provide public services. Allowing towns and cities another way to raise revenue would reduce municipalities' reliance on the problematic property tax.

More details on these proposals are provided later in this testimony.

### Property Tax Dependence

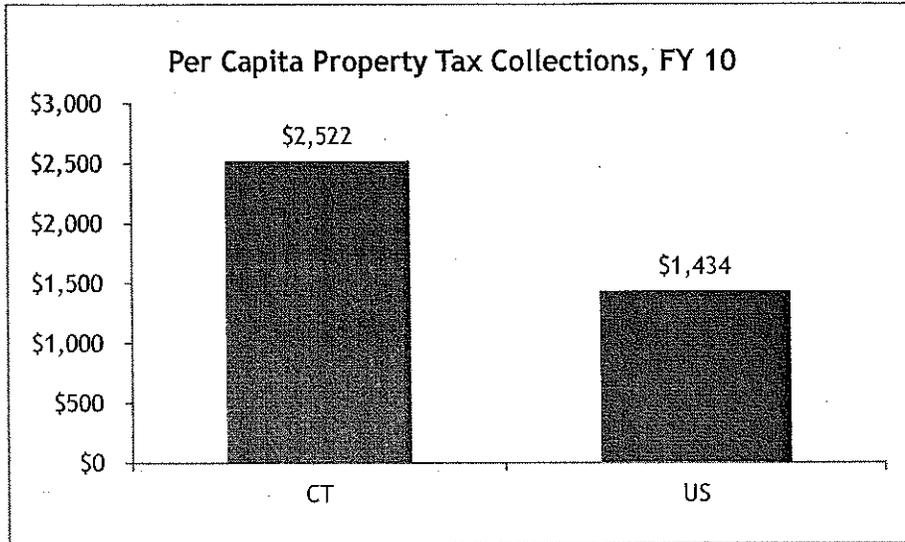
The property tax is the single largest tax on residents and businesses in our state. The property tax is income-blind and profit-blind. It is due and payable whether a resident has a job or not, or whether a business turns a profit or not.

The property tax levy on residents and businesses in Connecticut was \$9.5 billion in 2013.<sup>1</sup>

The per capita property tax burden in Connecticut is \$2,522, an amount that is almost twice the national average of \$1,434 -- and 3rd highest in the nation. Connecticut ranks 8<sup>th</sup> in property taxes paid as a percentage of median home value (1.70 percent for Connecticut vs. 1.14 percent for the US).<sup>2</sup>

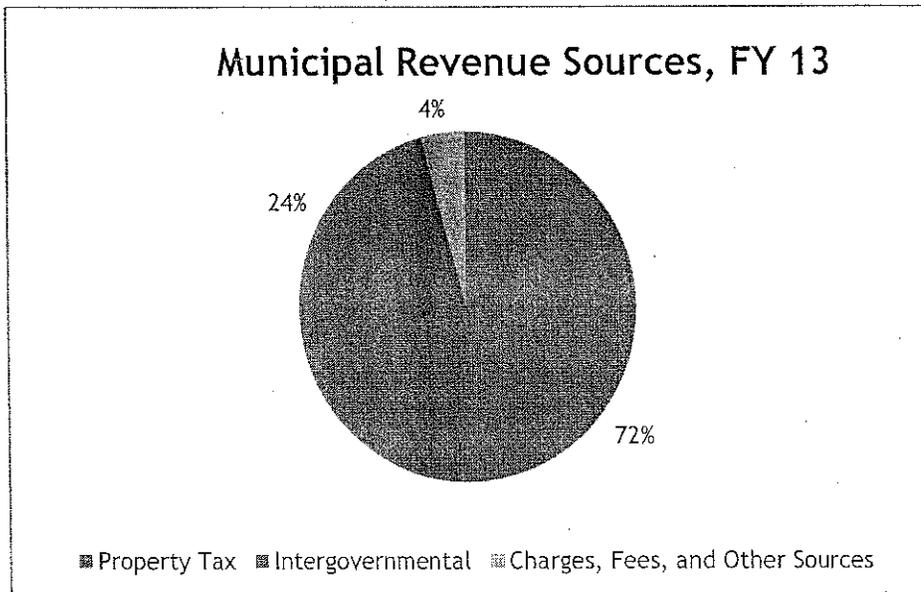
<sup>1</sup> OPM, *Municipal Fiscal Indicators*, 2009-2013

<sup>2</sup> Tax Foundation, 2010 Data



Source: Tax Foundation

Statewide, 72 percent of municipal revenue comes from property taxes. Most of the rest, 24 percent, comes from intergovernmental revenue, mostly in the form of state aid. Some Connecticut municipalities are almost totally dependent on property taxes to fund local government. Fourteen towns depend on property taxes for at least 90 percent of all their revenue. Another 54 municipalities rely on property taxes for at least 80 percent of their revenue.<sup>3</sup>



Source: OPM *Municipal Fiscal Indicators, 2009-2013*; Does Not Include "Other Financing Sources"

Connecticut is more dependent on property taxes to fund local government than any other state in the nation.<sup>4</sup>

<sup>3</sup> OPM, *Municipal Fiscal Indicators, 2009-2013*

<sup>4</sup> Based on data from the US Census Bureau and the Tax Foundation

Connecticut is also the most reliant state in the nation on property taxes to fund preK-12 public education.<sup>5</sup> That means that the educational opportunity of a child in our state is directly tied to the property tax wealth of the community in which he or she lives.

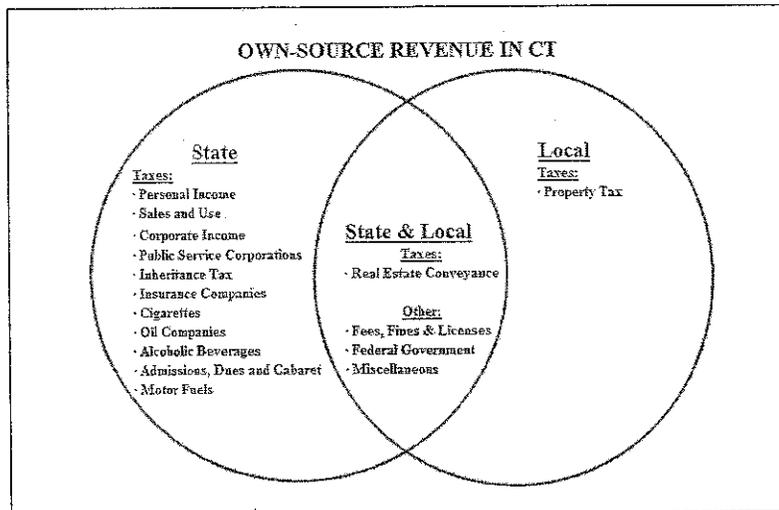
**The Property Tax**

- Connecticut's biggest state-local tax
- Regressive: Income/profit blind
- Property and income wealth vary widely from town to town in Connecticut
- Connecticut is more dependent on it than any other state
- Biggest tax on Connecticut businesses
- 72% of all municipal revenue
- Primary funder of PreK-12 public education in Connecticut

The property tax accounts for 37 percent of all state and local taxes paid in our state. In FY 13, Connecticut businesses paid over \$700 million in state corporate income taxes, but over \$1 billion in local property taxes.<sup>6</sup>

**Why is Connecticut so Reliant on the Property Tax?**

The revenue options available to Connecticut towns and cities are limited by state statute. The property tax is the only tax over which municipalities have significant authority. Municipalities can levy a conveyance tax on real estate transactions, but that tax rate is set by the State and provides a relatively small amount of revenue. That rate (0.25%) has remained the same since 2003.



Source: CCM 2014

<sup>5</sup> CCM estimate based on data from US Census Bureau, *Public Elementary-Secondary Education Finances, 2012*

<sup>6</sup> CCM estimate

Similarly, municipalities can levy user fees and charges to cover some of the costs of providing services. These are again limited by state law and cannot be used to raise revenue, only to cover necessary costs.

All of this means that, in terms of generating own-source revenue, Connecticut towns and cities are effectively restricted to the regressive and antiquated property tax.

### ➤ PROPOSAL: FULLY FUND PILOTS

When individuals work in or visit hospitals, attend or work in colleges, visit museums, or attend concerts, they take advantage of the services of a host municipality. Patrons, workers, and the tax-exempt institutions enjoy police protection, use of roads and sidewalks, garbage collection, sewerage, and the entire range of services funded from local property taxes. But, because of state-mandated exemptions, no property tax dollars are available from these institutions to finance the local services that support them.

When the State provides less than 100% reimbursement for the loss in revenue that results from these property tax exemptions, residents and businesses in the municipalities where these exempt properties are located must pay for (subsidize) the services used by others.

Because all state residents benefit in one way or another from the existence of tax-exempt institutions and from the services provided by their host municipalities to support them, all state residents should share the cost burden. State reimbursement for these exemptions -- funded from the many sources of revenue paid to the State by individuals and businesses -- is the appropriate mechanism for ensuring that host municipalities, and their residential and business property taxpayers, are made whole.

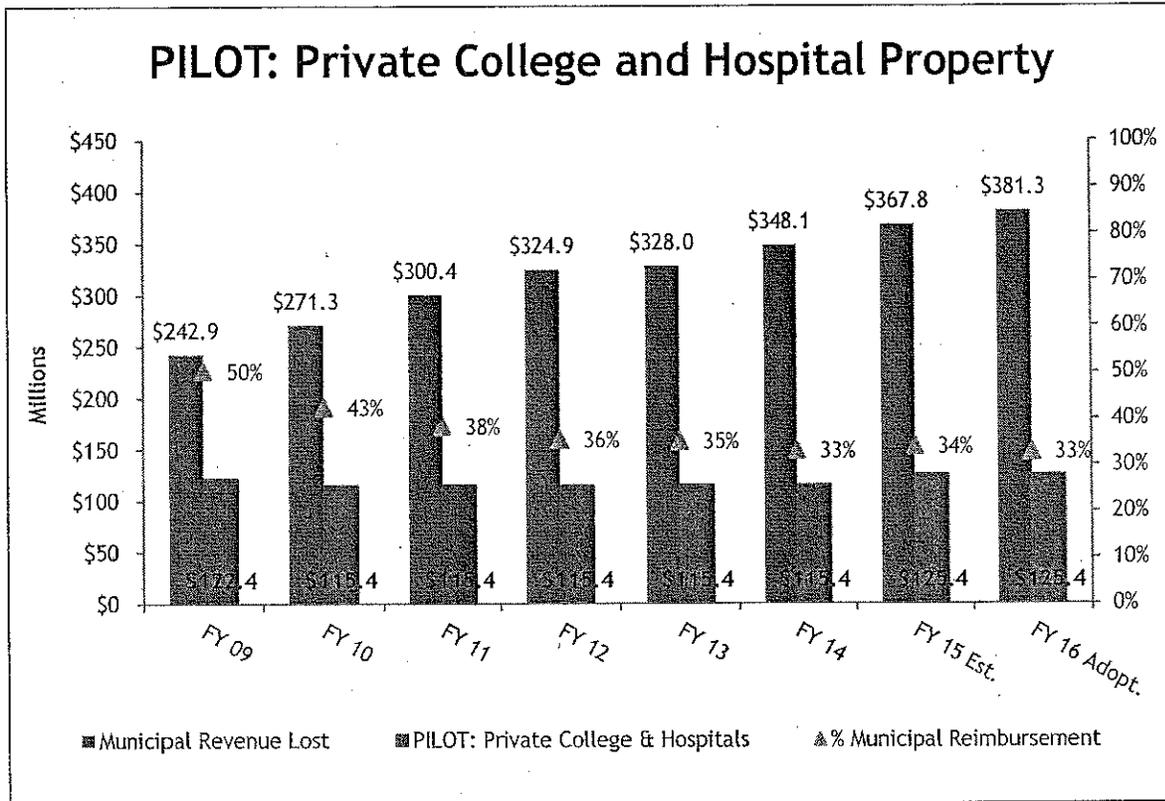
Appendix A lists the 77 state mandated property tax exemptions.

#### **PILOT: Private Colleges & Hospitals**

Municipalities receive payments in lieu of taxes (PILOTs) from the State as partial reimbursement of lost property taxes on state-owned and on private college and hospital property. This lost revenue totals about \$700 million.<sup>7</sup> The reimbursement rate for tax-exempt private college and hospital property is supposed to be 77 percent. It is actually 33 percent.

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<sup>7</sup> CCM estimate. PILOT reimbursements cover only *real* property and do not include revenue lost from state-mandated exemptions on *personal* property.



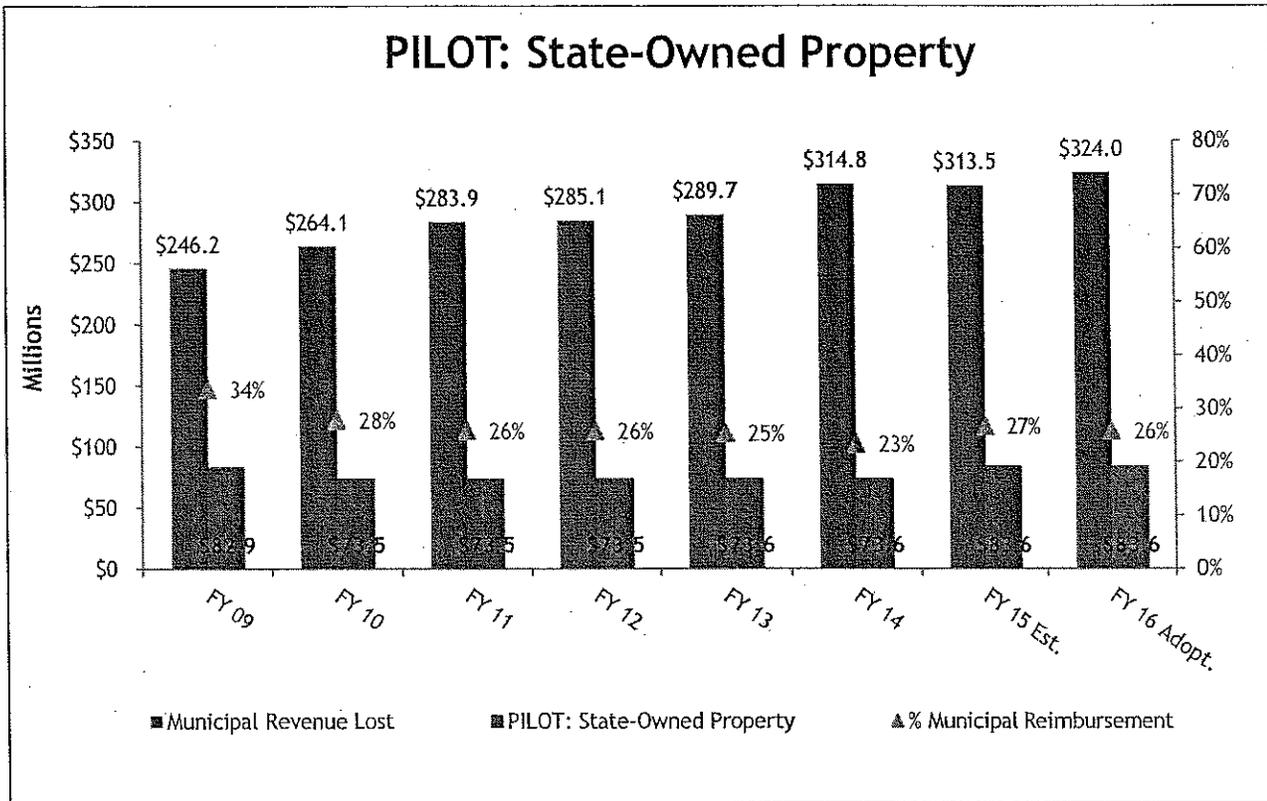
Source: Adopted state budgets; CCM

Note: This includes only revenue lost on real property and not additional revenue lost on personal property.

The 2015 General Assembly did pass a law wherein real property that a “health system” acquires on or after October 1, 2015, and personal property related to services delivered at the property will be taxable, if that property was taxable at the time of acquisition. This applies to health systems that had, for the 2013 fiscal year, at least \$1.5 billion in net patient revenue from facilities located in the state. While appreciated and helpful, the law is prospective.

**PILOT: State-Owned Property**

Similarly, the reimbursement rate for most state-owned property is supposed to be 45 percent. It is actually 26 percent. The actual reimbursement rates are lower due to statutes that allow the amount of the PILOT reimbursements to be reduced on a pro-rated basis when state appropriations are not sufficient. In addition, these PILOT reimbursements cover only *real* property and do not include revenue lost from state-mandated exemptions on *personal* property. Many of our poorer towns and cities host the most tax-exempt property.



Source: Adopted state budgets; CCM

Note: This includes only revenue lost on real property and not additional revenue lost on personal property.

### Percentage of State Tax Revenue

Municipal officials -- and their property taxpayers -- appreciate the 2015 General Assembly allocating 0.5% of sales tax revenue to towns and cities (also, a cap was placed on property taxes for motor vehicles). However, *a property tax cap was also imposed* – with insufficient exemptions for towns. CCM proposed exemptions that surrounding states included in caps, but they were not incorporated by the Legislature.

CCM is concerned that what’s past is prologue, so towns are reticent. The State has made numerous revenue promises to municipalities that weren’t kept (the PILOT for manufacturing machinery and equipment and the Municipal Revenue Sharing Account, for starters). Further, the State is facing a \$1 billion plus revenue shortage for FY 18. Will the sales tax revenue to towns survive? Past history says no.

### ➤ PROPOSAL: MEET STATE OBLIGATION TO FUND PUBLIC EDUCATION

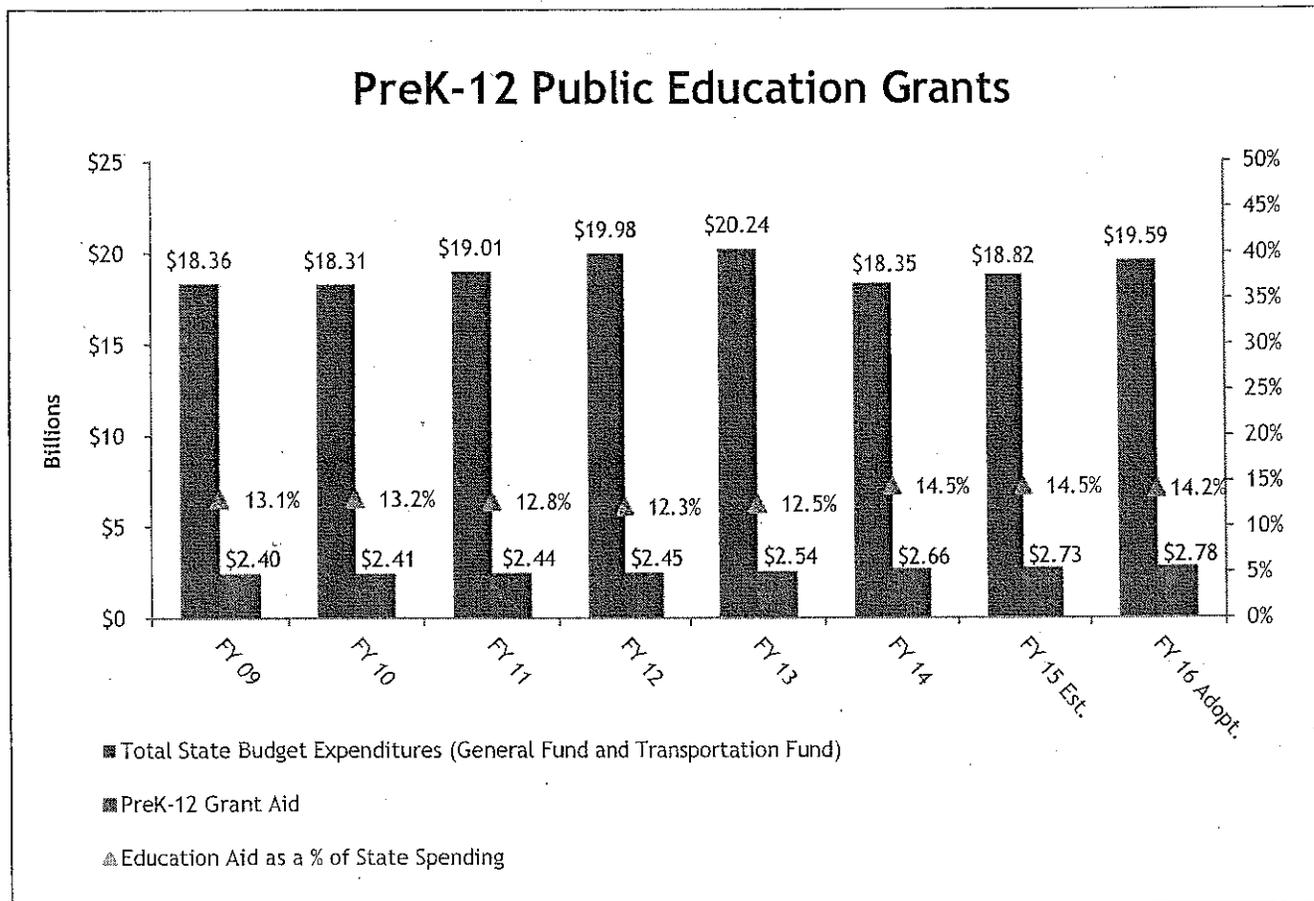
At least an equal partnership between state and local revenue sources has been a longstanding goal of the Connecticut State Board of Education. In 1989-90, the state share of total education costs reached 45.5 percent, the closest it has ever come to that goal.<sup>8</sup> Any movement toward that mark is important because additional state dollars can reduce dependence on property taxes and lessen the inequity in education funding.<sup>9</sup>

<sup>8</sup> State Department of Education (SDE)

<sup>9</sup> More details on education finance will be provided in an upcoming CCM policy report.

**Education Aid**

Statewide, 59 percent of municipal budgets go to pay for preK-12 public education. At \$7.8 billion in FY 13, preK-12 public education is the single most expensive municipal service in Connecticut.<sup>10</sup>

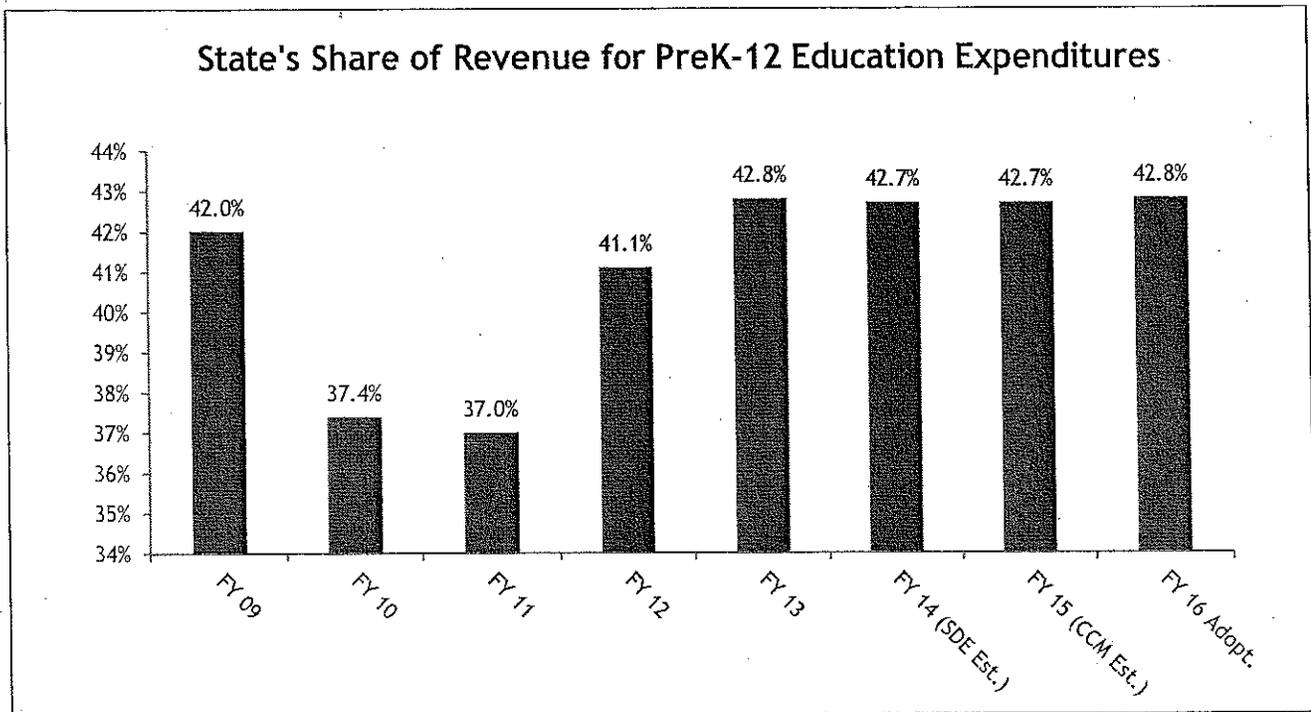


Source: Adopted state budgets; CCM

Note: Total state budget expenditures are reduced in FY 14 due to the removal of the federal share of the Medicaid appropriation totaling approximately \$2.8 billion.

Education aid to municipalities is expected to be \$2.8 billion in FY 16, 85 percent of total state aid to towns and cities.

<sup>10</sup> OPM, *Municipal Fiscal Indicators, 2009-2013*



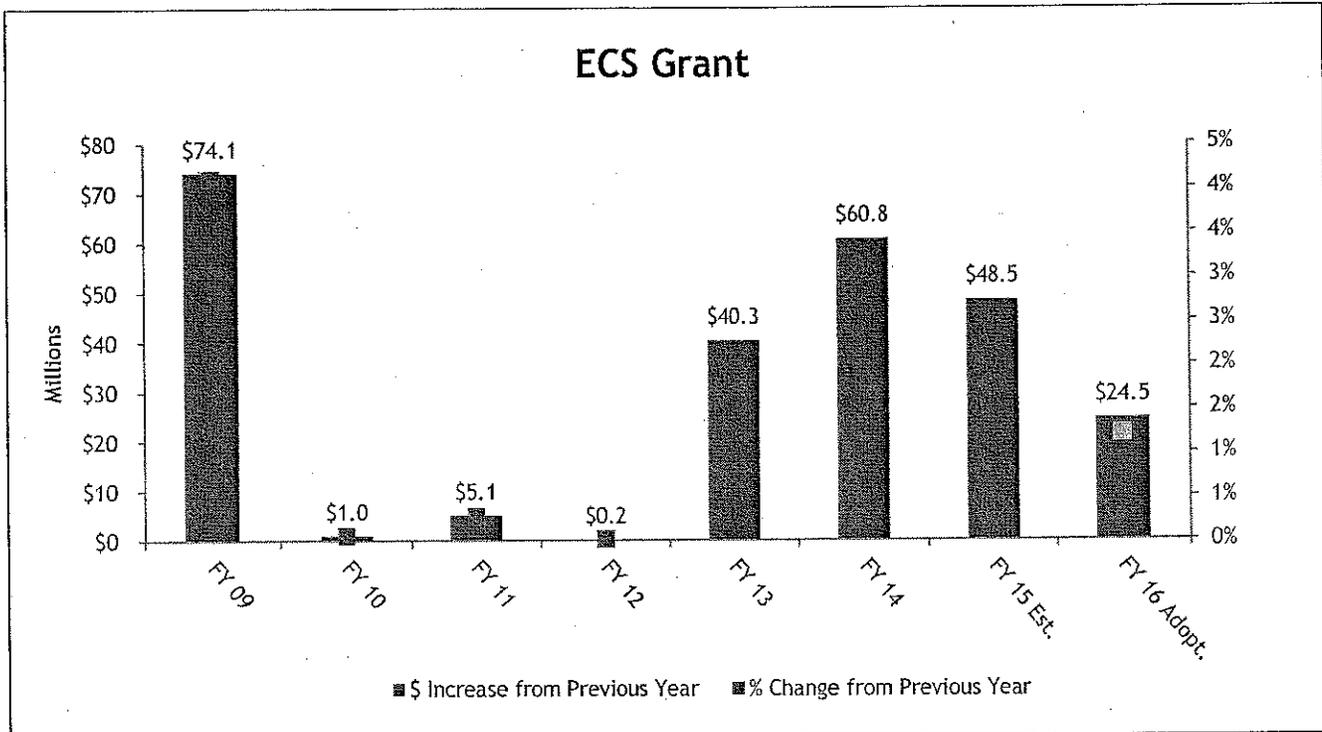
Source: State Department of Education; CCM estimates

### Education Cost Sharing (ECS)

The ECS grant is the State's largest general education assistance grant. It will total \$2.06 billion this year. While the recent increases in ECS are welcome, they do little to address the chronic underfunding of ECS. The ECS grant is currently underfunded by more than \$600 million, and amount that would be shown to be even greater under a proper adequacy study.<sup>11</sup>

The education reform initiatives enacted in 2012 were not accompanied by significant increases in new state dollars. More will be asked of struggling districts in order to leverage modest increases in education aid.

<sup>11</sup> CCM estimate based on SDE data for 2014-15



Source: Adopted state budgets; State Comptroller reports

Note: Since FY 13, ECS totals include charter school funding that was moved into the ECS account.

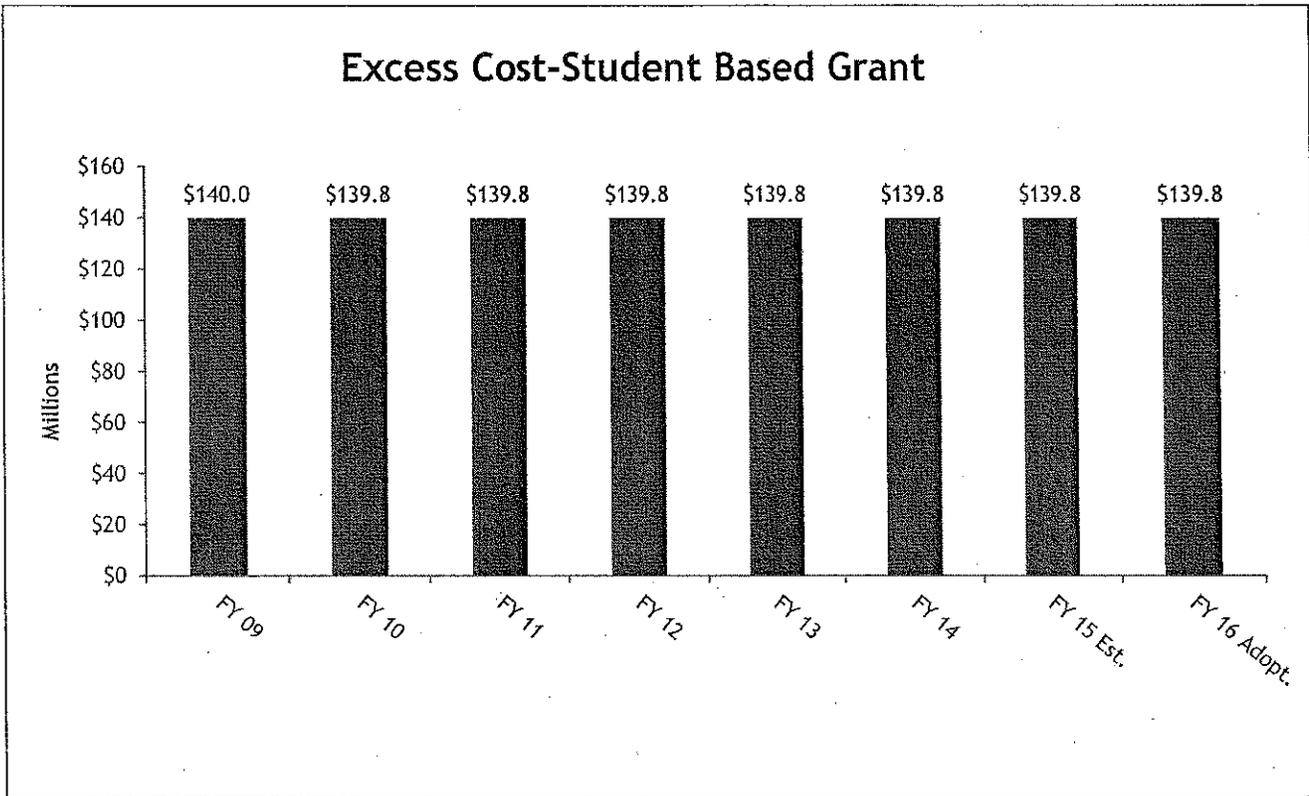
#### Special education

Special education is a significant cost driver for local government. These costs now surpass the \$1.8 billion mark statewide. This spending accounts for about 22 percent of total current expenditures for education in Connecticut, and annual costs have been growing as much as six percent in recent years.<sup>12</sup>

The State provides the Excess Cost-Student Based grant to help reimburse municipalities for the costs of special education. The grant provides a circuit breaker once the expenditures for a student exceed a certain level, currently 4.5 times the per pupil spending average of the district. So, for example, if a municipality spends an average of \$10,000 per pupil, it must spend at least \$45,000 for a special-education student before being eligible for any state reimbursement.

Unfortunately, the grant has been level-funded for seven years. This means that the state reimbursement has not kept pace with the escalating costs of special education. Without full funding, towns and cities are forced to find other ways to pay for special education. Not surprisingly, the burden falls on residential and business property taxpayers and non-education services.

<sup>12</sup> SDE, 2013-14 data



Source: Adopted state budgets; State Comptroller reports

➤ **PROPOSAL: PERMIT MUNICIPAL REVENUE DIVERSIFICATION**

As mentioned earlier, Connecticut is one of only 15 state that allows municipalities just the property tax. Allowing towns and cities another way to raise revenue would reduce municipalities' reliance on the problematic property tax. It could help sustain municipalities and add more certainty to local budgets.

There are primary ways that this can be dealt with:

**1. Local Option Taxes**

Allow distressed municipalities to **levy certain types of local-option taxes** as a way to take pressure off of property taxes. For example, locally levied sales taxes and hotel-occupancy taxes can be considered in municipalities where those industries are strong.

**2. Make local taxes applicable statewide**

One very straightforward approach would be for the State to add new sources of municipal revenue, but do so on a *statewide* basis. In this way all municipalities would be able to relieve pressures on the property tax, while avoiding any competitive harm that would arise if only certain municipalities applied the tax.

For example, the State could authorize all municipalities to collect a local tax on lodging. The money would be kept by any municipality with a hotel, motel, B&B, etc. One attractive aspect of hotel taxes is that they export most of the tax to out-of-state visitors, rather than place the revenue burden on locals.

### Summary

If the State wants to ensure its economic competitiveness, it must start with sustaining its towns and cities. Funding critical local public services come from two primary sources – the property tax and state aid, and it is increasingly clear that sustaining state aid is an essential component to thwarting the municipal over-reliance on the property tax.

CCM urges the Panel to stand strong for residential and business property taxpayers by building on the work of the General Assembly to provide meaningful, predicable and sustained property tax reform.

Thank you.

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If you have any questions, please call Ron Thomas ([rthomas@ccm-ct.org](mailto:rthomas@ccm-ct.org); 203-498-3022), George Rafael ([grafael@ccm-ct.org](mailto:grafael@ccm-ct.org); 203-928-9077) or Randy Collins ([rcollins@ccm-ct.org](mailto:rcollins@ccm-ct.org); 860-707-6446).

## APPENDIX A:

### STATE MANDATED PROPERTY TAX EXEMPTIONS

The following property is exempt from taxation in Connecticut (C.G.S. §12-81):

1. Property of the United States.
2. State property, reservation land held in trust by the state for an Indian tribe.
3. County Property (repealed).
4. Municipal Property.
5. Property held by trustees for public purposes.
6. Property of volunteer fire companies and property devoted to public use.
7. Property used for scientific, educational, literary, historical or charitable purposes.
8. College property.
9. Personal property loaned to tax-exempt educational institutions
10. Property belonging to agricultural or horticultural societies.
11. Property held for cemetery use.
12. Personal property of religious organizations devoted to religious or charitable use.
13. Houses of religious worship.
14. Property of religious organizations used for certain purposes.
15. Houses used by officiating clergymen as dwellings.
16. Hospitals and sanatoriums.
17. Blind persons.
18. Property of veterans' organizations.
  - a. Property of bona fide war veterans' organization.
  - b. Property of the Grand Army the Republic.
19. Veteran's exemptions.
20. Servicemen and veterans having disability ratings.
21. Disabled veterans with severe disability.
  - a. Disabilities.
  - b. Exemptions hereunder additional to others. Surviving spouse's rights.
  - c. Municipal option to allow total exemption for residence with respect to which veteran has received assistance for special housing under Title 38 of the United States Code.
22. Surviving spouse or minor child of serviceman or veteran.
23. Serviceman's surviving spouse receiving federal benefits.
24. Surviving spouse and minor child of veteran receiving compensation from Veteran's Administration.
25. Surviving parent of deceased serviceman or veteran.
26. Parents of veterans.
27. Property of Grand Army Posts.
28. Property of United States Army instructors.
29. Property of the American National Red Cross.
30. Fuel and provisions.
31. Household furniture.
32. Private libraries.
33. Musical instruments.
34. Watches and jewelry.
35. Wearing apparel.
36. Commercial fishing apparatus.
37. Mechanic's tools.
38. Farming tools.
39. Farm produce.
40. Sheep, goats, and swine.
41. Dairy and beef cattle and oxen.
42. Poultry.

43. Cash.
44. Nursery products.
45. Property of units of Connecticut National Guard.
46. Watercraft owned by non-residents (repealed).
47. Carriages, wagons, and bicycles.
48. Airport improvements.
49. Nonprofit camps or recreational facilities for charitable purposes.
50. Exemption of manufacturers' inventories.
51. Water pollution control structures and equipment exempt.
52. Structures and equipment for air pollution control.
53. Motor vehicle of servicemen.
54. Wholesale and retail business inventory.
55. Property of totally disabled persons.
56. Solar energy systems.
57. Class I renewable energy sources and hydropower facilities.
58. Property leased to a charitable, religious, or nonprofit organization.
59. Manufacturing facility in a distressed municipality, targeted investment community, or enterprise zone.
60. Machinery and equipment in a manufacturing facility in a distressed municipality, targeted investment community, or enterprise zone.
61. Vessels used primarily for commercial fishing.
62. Passive solar energy systems.
63. Solar energy electricity generating and cogeneration systems.
64. Vessels.
65. Vanpool vehicles.
66. Motor vehicles leased to state agencies.
67. Beach property belonging to or held in trust for cities.
68. Any livestock used in farming or any horse or pony assessed at less than \$1000.
69. Property of the Metropolitan Transportation Authority.
70. Manufacturing and equipment acquired as part of a technological upgrading of a manufacturing process in a distressed municipality or targeted investment community.
71. Any motor vehicle owned by a member of an indigenous Indian tribe or their spouse, and garaged on the reservation of the tribe (PA 89-368)
72. New machinery and equipment, applicable only in the five full assessment years following acquisition.
73. Temporary devices or structures for seasonal production, storage, or protection of plants or plant material.
74. Certain vehicles used to transport freight for hire.
75. Certain health care institutions.
76. New machinery and equipment for biotechnology, after assessment year 2011.
77. Real Property of any Regional Council or Agency.