

Testimony of Paul Cillo, Public Assets Institute
On Draft Request 15-1034, draft 2.1; 2/12/15; 9:42 pm

Mr. Chairman, members of the committee. My name is Paul Cillo. I'm the president of Public Assets Institute, a nonpartisan, nonprofit public policy think tank here in Montpelier.

As I've noted in my previous testimony before this committee, I am not an expert on education policy. Public Assets' work and our expertise is on tax, budget, and economic policy. So my comments today will focus on fiscal issues with the draft education funding legislation being considered by the committee, specifically drafting request 15-1034, draft 2.1 dated 2/12/15 at 9:42 pm.

Secs. 2,3,4,5 & 6 Yield; Dollar Equivalent; Property tax adjustment lag/withholding

1. Yield; dollar equivalent: We support the intention of this draft to more accurately describe the Legislature's annual process of calibrating tax rates for the education funding system and to simplify this process so that the press and the public can understand it. And we think that pegging the system to the dollar equivalent and ensuring that taxes based on income and the nonresidential property taxes move in proportion to the dollar equivalent is the right approach.
 - a. However, the current draft doesn't do this. Instead of establishing a proportional relationship of taxes among the various tax payer groups, it sets a proportional relationship among tax rates, which creates unnecessary and unfair distortions.
 - b. We recommend that the Legislature set the dollar equivalent for the homestead tax and then set the income rate and nonresidential rate so that the median income, median homestead property, and median non-residential tax will have the same proportional change each year.
2. Property tax adjustment lag/withholding:
 - a. We want a system that is understandable and fair. Our current system is neither.
 - b. We calculate this year's rebate based on last year's budget vote and the income from the year before last, so the bill that a taxpayer gets after their budget vote has little to do with that vote.
 - c. The system would work better if it use the current year's budget and school tax rates and last year's income (the income taxpayers are filing by April this year).
 - i. This makes it possible for school district voters to understand the tax consequences of their vote for school spending.
 - ii. Under this scenario, it would be best if the state sent a separate bill for the income-based tax so that it isn't confused with the property tax.

Secs. 7 & 8 Ballot language; Per-pupil spending

1. Two-vote requirement: This was a bad idea from the beginning. It's confusing to voters and it's a good idea to repeal it.

2. Form of school budget ballot question: We think it is a great idea and long overdue to include the education spending per equalized pupil in the ballot question.
 - a. In addition to the percentage higher or lower than the previous year, we recommend including the percentage the current proposal is above or below the statewide average for the current year.

Secs. 9, 10 & 11 Small school support

1. Only comment here is that small school support was not part of Act 60. It was an amendment that was added in the years following passage in 1997.
2. The Legislature has sent a mixed message about small schools
 - a. On one hand, small schools are seen as a desirable part of the education system and a center of community life in Vermont
 - b. On the other hand, they're viewed as inefficient, not providing opportunities that students need in the 21st century
 - c. While we have not done any research about small schools, we think the committee needs to be clear about the facts about cost and performance of small schools in Vermont before it takes action like that proposed in this bill. Closing small schools will likely have negative consequences on community life in Vermont, which may in turn have negative consequences for the students from those communities.
3. It hasn't been clear in the public debate what students we're talking about in small schools. Is there any difference in how young students are viewed vs. older students in whether they are likely to be better educated in town or at a regional school?

Secs. 12 & 13 Declining enrollment; equalized pupils; 3.5 percent limit

1. The 3.5 percent cap on the decline in the number equalized pupils for individual school districts in any year was not part of Act 60. It was an amendment that was added in the years following passage in 1997.
2. The reason it was enacted was that some districts, especially small districts, were seeing fluctuations in the number of students and therefore in education spending per pupil and school tax rates. In small districts even small fluctuations can have a dramatic effect on tax rates.
3. So this "hold harmless" provision was enacted as a way to prevent the yo-yo effect in tax rates.
4. Again we haven't analyzed the data on fluctuations in tax rates, but recommend that the committee get that analysis before including this provision to avoid creating another problem that your constituents will complain to you about: the sharp increase in tax rates from a one or two-year drop in student count.
5. Also keep in mind that eliminating this hold-harmless provision doesn't do anything to reduce the cost of education and it involves such a small amount of money, it's unlikely to have any impact on property taxes.

Sec. 14 Special education funding; average daily membership

1. There is nothing in the draft about ADM. Is the committee considering a change related to ADM?

One additional point: I noted in Title 32 section 6066 relating to calculation of the income sensitivity adjustment, there is the provision that anyone getting an adjustment must also pay school property taxes on their homes value above \$500,000. From the beginning when this provision was enacted several years ago, it has created confusion and unfairness for tax payers, especially for retired Vermonters. We think it should be repealed as you are thinking about changes this year.

Those are the extent of my comments about the draft before the committee.

The chair asked that I also comment on the concept of a shift to an income-based tax for schools.

As I indicated in my previous testimony before this committee, we think that it is time to eliminate the school property tax on primary residences, which would also eliminate a number of nagging problems that the committee is wrestling with:

1. Complexity and confusion for taxpayers:
 - a. The common level of appraisal adjustment: the adjustment is made to property tax rates rather than property value, which is incomprehensible to taxpayers and undermines a basic understanding of the fairness of the system: same tax rate for the same per-pupil spending.
 - b. Property tax bills that taxpayers don't actually pay: School tax bills arrive as property tax bills with school and municipal taxes together. The adjustment on the bill from the state is incomprehensible, though it is supposed to represent the difference between paying based on property and paying based on income.
 - c. Multiple rates for the same spending decision: Voters should be able to do the math in their head at town meeting when they're asked to vote on school spending. That's currently impossible. There's the property tax rate on their home, there's the income tax rate on their household income, there's both if they have a housesite valued at more than \$500,000; and there's neither if the adjustment reaches the Legislature's arbitrary cap.
2. Fairness:
 - a. The school property tax is regressive, even after income sensitivity is applied. Based on Tax Dept analysis from 5 years ago, the median school tax bill on a homestead for someone with income of a \$1 million is .5 percent of income. Taxpayers who pay based on income pay more than 5 times that portion of their income. Having all taxpayers pay based on income would make the system less regressive.
 - b. Since the 1970s the Legislature has recognized that income is a fairer way to assess school taxes primarily because it is income that Vermonters use to pay their taxes. As people move into Vermont and push up property values, Vermonters paying a property tax on their homes are faced with higher and higher tax burdens as a percentage of their income. Moving to school taxes on homes based on income would eliminate the pressure on Vermonters to sell their homes and maintain diversified communities.
3. Property no longer makes sense as a way to determine contribution level to education.
 - a. We're recommending that you eliminate the school property tax on primary residences. Nonresidential property would still be taxed based on property

value mainly because it's not practical to use an income tax for this class of property.

- b. Property did make sense in the 18th century when property, not income, was the measure of a person's ability to pay. After the industrial revolution, there was a shift in the US and in VT away from a land-based economy toward a paycheck working in mills, machine shops, manufacturing businesses. At the beginning of the 20th century, the income tax was started in the US, reflecting this economic shift.
- c. It's long overdue for Vermont to move the rest of the way to income and shift off the school property tax for primary residences.