H.538 Tax Renewal Bill Memo 1/10/18 **House Ways & Means Committee**
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There are three key ways in which the Vermont tax code does not work as well as it might for Vermonters. The tax code is quite complex, especially the property tax assistance process, and this can make it hard for taxpayers to fulfill their obligations properly; it can also make it hard for citizens to have confidence that all are paying their fair share. The tax code violates the principles of horizontal and vertical equity, because the use of itemized deductions and the functioning of the education finance system can mean that people in similar situations pay different amounts of taxes and people with more resources do not pay more in taxes than those with less. One policy goal of the tax system is to support access to housing, yet a substantial portion of the resources used for income tax deductions and property tax assistance go to taxpayers who clearly have the ability to afford housing.

PROPOSAL:

The aim of this proposal is to renew the tax code for the income tax and the property tax in a way that is simpler, more transparent, more equitable, and more effective in achieving certain policy goals. This is done by:

(1) broadening the income tax base by using as the tax base Adjusted Gross Income instead of Taxable Income – this means removing most pass through Federal deductions -- and by including the value of employer paid premiums in the tax base, which will result in a "tax renewal dividend" to be used mostly to lower tax obligations with tax credits;
(2) removing the costs of the income sensitivity and current use programs that are not directly connected to education from the Education Fund, which will mean that property tax rates can be reduced significantly;
(3) using almost all of the "tax renewal dividend" from broadening the tax base to fund a standard tax credit for ALL Vermont filers, which will be supplemented at the lower income levels by an additional refundable housing credit to replace Income Sensitivity property tax assistance and the renters rebate, and using a small part of it to fund the Current Use program in the General Fund;
(4) to prevent a surge in property tax rates after the reduction in the base rates a rate of growth cap would be imposed on the total cost of teacher and staff compensation that is linked to the growth rate of Vermont gross domestic product or some other appropriate measure.

BENEFICIAL RESULTS:

The results of this approach are illustrated in examples below, and although due to limitations of skill, time, and access to updated and sorted numbers there is a lot of estimation and extrapolation, the basic pattern is clear. It looks as if it would be possible to do the maneuvers described above. The results show that it may be possible to:

(1) Base property tax rates come down significantly, all taxpayers get the same standard credit, and then housing support credits are awarded based on income;
(2) Ensure that people in similar situations in terms of income or property value will pay similar amounts in taxes (allowing for variations in local school tax rates) – this improves horizontal and vertical equity;
(3) Award assistance with housing based on income alone rather than also according to home value or having a mortgage – in this way support for housing is targeted on lower and middle income Vermonters rather than also supporting higher income taxpayers through the availability of the mortgage interest deduction and the real estate property tax deduction along with the upper reaches of Income Sensitivity;

(4) Re-connects school budget votes to property tax rates again, because since housing assistance is through an income tax credit so that the expected rate for school budgets will be paid by all;
(5) Tax obligations will shift around in this approach: anyone with relatively high income who used a lot of itemized deductions will likely pay more in income taxes, but if they own a homestead or nonresident property they will pay less in property taxes – there is no intent to make those changes even out;
(6) By removing Current Use and Income Sensitivity from the Education Fund this shifts some of the costs into the General Fund and onto the Income Tax system respectively, and this in effect means that part of the burden that had been on the property tax has been shifted onto the income tax, which has long been a policy goal of some;

CAVEATS RE NUMBERS AND EXAMPLES:

(1) The illustrative examples are chosen for simplicity based on data available to me as an individual legislator – in no way is this the kind of rigorous analysis that the Joint Fiscal Office can do for us;
(2) In order to explore the possibilities of this approach I estimate or extrapolate from available numbers – in no way are the results conclusive, they simply demonstrate what might be possible;
(3) There is an issue in terms of how to treat Vermont residents and residents of other states within the tax code – according the Peter Griffin of Legislative Council it should be possible to create a Vermont homeowner credit in the Income tax system just as we did have a Vermont homestead declaration and property tax assistance now, and it may be possible to allocate the standard credit based on whether the majority of a taxpayer's income was earned in Vermont;
(4) In my examples I use tax credits to distribute the Tax Renewal Dividend within the income tax system because at the lowest level rate reductions don't mean much – there has to be a refundable tax credit – and because I am unable to do the complex calculations of how allocate the money to rate reductions, but above the lower income levels it might make sense to do a rate reduction instead of a credit;
(5) In the changes made in the Vermont income tax I am not touching all of the Vermont specific provisions – just eliminating the Federal pass through standard and itemized deductions and replacing them with a standard credit and a housing credit; some of the other Federal credits could be replaced in some way.

***** RESULTS OF ILLUSTRATIVE NUMERICAL EXAMPLES *****

Bearing in mind all the cautions listed above, the examples I have developed to illustrate the basic approach below lead to the following conclusions:

***Total Education Fund costs are reduced by $225 million because of the removal of Current Use, Income Sensitivity, and Renter Rebate costs.**
***Base Homestead Education Property tax rates will be reduced by 34 cents.**
***Base Non Resident Education Property tax rates will be reduced by 5 cents.**
***Total Property Taxes are reduced by $225 million.**
***The Net Increase in Total Income Taxes is $25 million through broadening the tax base by eliminating the Federal itemized and standard deduction and ending the exemption for the value of employer provided benefits.**
***The Net increase in Total General Fund spending is $25 million to partially fund Current Use in GF.**
***The broadening of the income tax base in this way will generate $300 million in additional revenue, which will be used to partially fund Current Use with $25 million, and then $275 million is used to fund a standard tax credit and a housing tax credit to replace the Income Sensitivity.**
***A standard tax credit will go to all Vermont filers.**
***A housing credit will go to low and middle income Vermont filers to replace the Income Sensitivity property tax assistance and renter rebate programs – given the decrease in Homestead property tax rate the size of this subsidy can be smaller, and its size is based on income not property value as well.**

*** The standard and housing credits will be funded with the $275 million of the additional funding from the broadening of the tax base.**
*** Some kind of circuit breaker program to support very low income Vermonters with housing may still be advisable.**
***The overall tax burden will be shifted from the Property Tax to the Income Tax.**
***The overall tax burden will be shifted towards higher income filers who lost itemized deductions and exemption of employer provided benefits, but the reduction in property taxes will mitigate this for many high earners who also own Vermont property.**
***Since Education Fund costs and property taxes both decline by $225 million, and General Fund spending and income taxes both rise by $25 million, THE NET CHANGE OF BOTH TAXES AND SPENDING IS A DECREASE OF $200 MILLION.**

(A) INCOME TAX RENEWAL: Broaden Base, Use Added Tax Revenue to Provide Tax Credits.

The basic approach to the income tax reform is to broaden the base and use most of the additional tax revenue to provide tax credits so that the net income tax revenue raised is slightly above what it would be beforehand. The Vermont tax base would shift from Taxable Income to Adjusted Gross Income, so that all the pass through federal deductions/credits/exemptions would go away, but the special Vermont credits/deductions would stay in place. Based on the current 2017 Biennial Tax Expenditures report, the total in foregone revenue for the federal pass thru deductions, including the Standard Deduction and everything, is $243 million from 2014. This reflects an amount AFTER the capping of the value of these itemized deductions at 2 ½ times the standard deduction, which was done in 2013. Since 2014 was three years ago I will use a value of $250 million as a current guesstimate.

These pass through deductions would continue to be available at the federal level unless altered by the federal tax changes currently in process. Nothing has been done to affect the Vermont specific income tax provisions.

I will also include in the tax base the value of benefits now being reported on the W-2 in the definition of income – add that to the AGI base. I think that this may include the value of health insurance premiums paid and retirement benefits contributions. All I have for Vermont at this time is a figure for just the health insurance premiums, which is an estimate from the 2011 Blue Ribbon Tax Structure Commission. On p.77 of the BRTSC report Bill Sayre in his minority recommendation uses $45 million as Vermont income taxes that might be assessed on the value of health benefits. Given that the $45 m number was from 2011, I will use $50 million in my sketch. But it should be borne in mind that if the value of all employer provided benefits were included this number would be higher. I believe that this change improves horizontal equity, since Vermonters who pay for their own health care premiums will be taxed the same as Vermonters whose employers pay those premiums for them. As it is now, Vermonters who do not have employer provided benefits in effect subsidize those who do, and who are not taxed on their value.

Including the value of these deductions and inclusions in income would mean that a taxpayer's income would increase by that amount. The impact on actual tax liability would then depend on the highest tax rate applied, with the increase in tax liability higher at the higher income levels and rates.

For instance, for a Single tax filer at the lowest tax bracket of .0355 (3.55%) the standard deduction of $6,300 has a value in terms of reducing tax obligation of around $223.65. For a Married Filing Jointly tax filer at the same tax rate bracket their standard deduction of $12,600 is worth around $447.30. For the same filing statuses at the highest tax rate bracket the standard deduction has values of $563.85 and $1,127.70, respectively. The same relative values would apply to a $6,300 or $12,600 value of the exemption from inclusion in income of employee provided benefit in reducing tax liability.

Although I do not have firm numbers in terms of the average value of itemized deductions taken overall or at particular income levels, the available data shows that many higher income taxpayers take thousands and thousands of dollars in deductions, which reduce tax liabilities by many times more than the standard deduction. Some of the itemized deductions in Vermont are now capped at a certain multiple of the value of the standard deduction, and they bump up against those caps, but some are not. This is why these Itemized Deductions create violations of horizontal and vertical equity in that it means that taxpayers at the same level of income before deductions pay very different tax obligations, and taxpayers at different levels of income could pay the same level of taxes. The Standard Tax Credits is not designed to fully replace the value of itemized deductions but those taxpayers who lose the itemized deductions may benefit from the reduction in property taxes that are determined below.

So the bottom line will be that I will have $300 million in revenue from broadening the tax base that would be realized at the CURRENT rates that I will use to create a Vermont standard credit on the income tax for all Vermont tax filers and a Vermont Housing Credit on the income tax for all Vermont filers below certain income levels. So $275 million is returned to taxpayers as tax credits immediately. The net increase in income tax revenues of $25 million will be used to fund the Current Use program in the General Fund to allow for the large reduction in property taxes.

See Section C below for the illustration of how this could work out.

[Note: An alternative approach would be to create a credit at the lower income levels and then to decrease the middle tax bracket rate in a way that would reduce tax liability by the same dollar amount for all filers except at the lower levels. More about that below. This is beyond my capacity given the numbers that I have at my disposal at this time.]

Income Tax Context:

Current Tax Base X Current Tax Rate = Current Tax Liability = Current VT Tax Revenue

Increased Tax Base X Current Tax Rate = Increased Tax Liability = Increased VT Tax Revenue
Increased Tax Liability = Current Tax Liability + Tax Renewal Dividend = Increased VT tax revenue
$300 million $25 million
Tax Renewal Dividend = Vermont Tax Credits + part of Current Use
$300 million = $275 million + $25 million

[Alternative Approach could be:
Tax Renewal Dividend = Vermont Tax Credit + Reduction in Tax Rate + part of Current Use]

(B) EDUCATION FUND & PROPERTY TAXES:
Current Use, Income Sensitivity, & other items Out & Reduce Property Tax Rates.

The process here will be to remove Current Use, Income Sensitivity, and other housing related supports from the Education Fund. The housing support policy goal will be accomplished through a Vermont residential or homeowner credit on the income tax. The Current Use program will be funded in the General Fund.

Current Use, Income Sensitivity, the Homeowner Rebate, and the Renter Rebate are removed from the Education Fund. Since they cost the EF about $45 million, $165 million, $7.3 m, and $8 m respectively, this removes about $225 million in costs from the EF. Most of these programs also have costs in the General Fund, which can now be collected and re-allocated to funding Current Use.

	Education Fund Share	General Fund Share
Income Sensitivity	**$164.1 m**	
Renter Rebate	**$8 m**	**$3.4 m**
Homeowner Rebate	**$7.3 m**	**$16.2 m**
Current Use	**$45 m**	**$11 m**
Totals:	**$224.4 m**	**$30.6 m**
ROUNDED FOR EASE OF CALCULATION:	**$225 m**	**$31 m**

(Sources: Preliminary Education Fund Outlook 2/27/17, numbers for FY2017, Joint Fiscal Office, and Biennial Tax Expenditure Report 2017.)

This means that $225 in costs have been removed from the Education Fund. Since a penny on the property tax rate is about $10 million, this could reduce both the homestead and the nonresident tax rates by about 22.5 cents, or it could be used to disproportionately reduce one or the other. It takes about $4 m to reduce the NonResident property tax rate by 1 cent. (Remember that this includes commercial, industrial, second homes, and land around primary homes beyond 2 acres. I will use $20 million of this to reduce the Non Resident Tax rate by 5 cents, to 1.48. It takes about $6m to reduce the HSTx rate by 1 cent. I will use $205 million to reduce the base homestead property tax rate of 1.00 by 34 cents to .66. This asymmetry is due to the fact that the Income Sensitivity and Homeowner Rebate programs were connected to supporting homeownership and they are the largest removed cost, so I will reduce the Homestead Rate the most in this sketch. The division of reductions could be done in other ways. (Note that we are currently setting the education YIELD rather than the base property tax rates, but by setting the yield we determine the average property tax rates, so I will continue to refer to property tax rates. If the total costs in the Education Fund are lower, property tax rates will be lower.)

Base Homestead Property Tax Rate reduced from 1.00 by 34 cents to .66 w/ $205 m @ $6 m per 1 cent
Base Nonresident Property Tax Rate reduced from 1.535 by 5 cents to 1.035 w/ $20 m @ $4 m per 1 cent
Cap rate of growth of remaining base education property tax rates/yields to prevent any burst of Education Spending by school districts given the lower rates.

All property tax adjustments related to these programs are taken out of the EF. This includes both the Income Sensitivity program and the Circuit Breaker, which is listed on the Education Fund Outlook as the Homeowner Rebate. These support programs will be eliminated and the policy goal of affordable housing will be achieved instead with a credit on the income tax which is refundable in the lower bracket. (See below.) This means that the cost of $164 million for Income Sensitivity comes out of the EF, but the cost of the Homeowner rebate of $7.2 million is also eliminated. The renter rebate is also eliminated, so there is no $7.4 million allocation in the Ed Fund. This add $14.6 to the reduction in costs in the EF, so that there is now about $225 million in total reduction.

Current Use will no longer be structured as a tax expenditure that is financed through foregone revenue in the Education Fund. The cost of this program will become a General Fund expenditure (as I believe that it was before the Ed Fund existed). The current cost is around $45 million, plus around $11 million in a current General Fund allocation to make the municipalities whole, for a total cost of $56 m. The cost of CU in the GF will be lower because of the reduction of the nonresident tax rate by about 5 cents from the current rate of 1.53, which will take about $20 million of the tax renewal dividend of $300 million. The new NR property tax rate of 1.48, this would be a reduction of about 3%, so the cost of the CU program in the GF would be less that it was before. I will set it at a total of $54 million.

The General Fund allocations to make up the difference to towns for the Income Sensitivity and the Renter Rebate, which add up to around $10 million, are no longer needed for those purposes. Those funds will be used to finance the Current Use program in the General Fund.

When the Income Sensitivity, Homeowner Rebate, and Renter Rebate programs are shifted into a tax credit on the income tax, this frees up the related GF costs of these programs, which are $3.2 m and $16.9 m respectively. So that means about $20 million in GF allocations available to finance the CU costs in the GF.

So to cover the $54 million CU costs in the GF, I can use the existing GF CU cost of $11 million that was going to the municipalities, add in the $20 m from the GF RR and HR allocations that are no longer needed, to give me around $21 m towards the $45 m GF CU cost. So I have a net cost of around $24 million in Current Use costs to cover in the General Fund. This will come from the Tax Renewal Dividend of $300 million. If I use $25 million to complete the financing of CU in the GF, I will have $275 million to use to create the Vermont Resident Credit. See below.

TO COVER CURRENT USE NEW TOTAL COST OF $54 MILLION IN THE GENERAL FUND

Existing GF CU cost of $11 m
Existing GF RR cost of $3.2 m
Existing GF HR cost of $16.2 m
Total: $30.6 m rounded to $31 m

Add $25 m from the $300 Tax Renewal Dividend

$31 m + $25 m = $56 million for Current Use costs. More than enough.

When the nonresident and homestead property tax rates are reduced as proposed above, it would be important that school districts should not see an opportunity to increase spending and therefore increase education property tax rates again. Therefore there should be some kind of temporary percentage cap on the rate of growth of those property tax rates, perhaps something like the rate of inflation plus 1%, to prevent a surge in spending that would again increase the property tax burden that has just been reduced.

(C.) TAX RENEWAL ALLOCATIONS
-- VERMONT STANDARD TAX CREDIT & HOUSING CREDIT EXAMPLE

I have $300 million from the Income tax reform shift from TI to AGI which eliminates all pass through federal deductions and the inclusion of employer provided health insurance premium benefits in the income tax base. I have to cover the net cost of $25 million for the Current Use, so I will take $25 million from that amount to be shifted as additional revenue to the General Fund (as above).

This leaves around $275 million in “tax renewal dividend” from the expansion of the income tax base to be used to finance a tax credit for all Vermont resident filers in some way.

But there is a Big Issue: how to do this legally/constitutionally given that fact that we have to be careful about treating residents and non-residents differently in the income tax. We might be able to make certain provisions available only to Vermonters if we framed it as a Homestead tax credit, like the Homestead tax and Income sensitivity, which is only available if residence and homestead is declared. Or we might be able to make certain provisions only applicable a taxpayer is a Vermont resident OR if a certain percentage of total income was from a Vermont source or if a person declares homestead or homeownership.

The $275 million divided by 321,000, the total number of Vermont filers of all statuses, would be an average $900 each – but this could be allocated in a different pattern of amounts to different categories of taxpayers. If it was impossible to create a restriction of tax credits/deductions to Vermont filers, the $275 million divided by 376,000, the entire number of income tax filers of all filing statuses including nonresidents, would mean an average of $700 each, which also could be allocated in different patterns.

It would be possible to allocate the Tax Renewal Dividend in a variety of ways. I will assume that the Vermonter/non-Vermonter is resolved through a provision about the source of the majority of income and the declaration of Vermont homeownership. Possible ways of proceeding from there would be a Standard Credit or Deduction, a low income housing tax credit, a renter credit, or a homeowner credit. This could also be done through reductions in tax rates, but such an adjustment is beyond my capacity due to the complexity of the interactions between the income to be tax and the tax brackets.

It is important to note that the manipulations here are just about the changes to the Federal pass through deductions and the employer paid benefits exemption. All of the Vermont specific income tax provisions like the Earned Income Tax Credit or the college saving credit and so forth are still in effect. I am just talking about changes to tax liability connected to the changes proposed here. All else is held constant.

Vermont Standard Tax Credit & Housing Tax Credit Example.

This tax credit has to be big enough to partly compensate for the loss of the standard deduction and the personal exemptions at the lower brackets, and it has to also function as a replacement for the income sensitivity property tax adjustment, and also extend some housing support to renters. It could be larger at the lowest tax bracket, and gradually be reduced at the higher tax brackets. The credit would be refundable in the lowest tax bracket, or part of it could be structured as a voucher that could be used to pay property taxes or rent.

The goal is to create a credit that will make it easier for Vermonters to pay for housing, so this partially replaces the Income Sensitivity and Homeowner Rebate and Renter Rebate program. These are no longer funded as property tax adjustments in the Education Fund. Since property tax rates are reduced significantly, it will be easier to pay them and some taxpayers might no longer be eligible for special support under the current program. The tax credit support will be provided based on the income and filing status of a taxpayer within the income tax as a tax credit. It is no longer based on property value or payment of mortgage interest or the number of people in a household.

Since I do not have access to the complex calculations within the current Income Sensitivity program that lead to different levels of state support for different income levels and property values, I cannot be sure how the support from the tax credits compares to it, and I do not claim that the example of tax credits below will fully replace that program for all taxpayers.

The reduction in the Homestead tax rate by 34 cents will be a different percentage reduction in rates depending on local education property tax rates. But I think that a 34 cent reduction should mean a $340 reduction in taxes owed on a $100,000 property, a $780 reduction in taxes owed on a $200,000 property, a $1,020 reduction in taxes owed on a $300,000 property, and so forth. Since property taxes owed are therefore reduced, homeowners do not need as big a state subsidy to be able to afford their property taxes and their homes.

The average Income Sensitivity support payment may be around $1,350. If the average property tax payment were to go down by about 20% (keying off the current average tax rate of around 1.52), the cost of the average support payment in the current Income Sensitivity program might go down by about $270. So the aim would be to be replacing something like a $1,000 level of support. It is worth noting that Income Sensitivity program is oriented towards Households, while this approach goes by income level tax filing status. So an actual household might end up combining several sets of tax credits, or it might not. In addition, this approach awards support based on income levels rather than also on property values, so some taxpayers who have valuable homesteads might receive less support overall than before.

I also do not have access to the calculations behind the special circuit breaker support program that helps when the combination of education and municipal property taxes is above a certain percentage. It appears to provide an average of another $658. Presumably if education property tax liability were reduced by about 20%, the needed payment here would also go down, perhaps by 20% or about $130. It looks as if it might still be necessary to have a special circuit breaker program for such homeowners, but it would cost considerably less.

Just for context, there are about 120,000 in Income Sensitivity Program (assuming Circuit Breaker recipients also counted in that total). There are about 320,000 Vermont Resident Filers in all statuses. The Homestead parcels are around 167,025, minus around 120,000, leaves around 47,000 homestead homeowners not in Income Sensitivity. There would therefore be around 164,000 renters. (Source: Tax Department Property Valuation Review Annual Report.)

So there is $275 million in tax renewal dividend to be used for this. There are about 320,000 Vermont resident filers (in all filing statuses or categories). This would mean a tax credit of about $900 for each such filer if done equally across the board. But I would want to adjust this credit for different income levels and filing statuses.

So I would propose a basic Vermont Resident Tax Credit in the amount of $300 for ALL Single Filers, and in the amount of $600 for ALL Married Filing Jointly, with ALL Married Filing Separately receiving $300, and with ALL Head of Household getting $450. This would be given to all income levels. This follows the proportions of the standard deductions, and it is not far from the value of the standard deduction at the lower tax brackets in terms of reducing taxes paid. (There are some other filing categories, but there are few returns there and I will set them aside for now – they would be handled according to the same principles. I am trying to avoid giving incentives for filing in one status or another.) To some extent the value of the standard credit is based on worth of standard deduction at the existing lowest tax rate bracket.

I would propose an additional Vermont Resident Housing Tax Credit that would be intended to function as a replacement for income sensitivity for homeowners and to also assist renters. This credit would be larger at the lower income levels, and also refundable. It would phase out after certain levels. The idea is that at higher levels many will be benefiting from the reduction in property taxes even if some formerly had income sensitivity.

***** NOTE: The original source of numbers for Vermonters of different filing statuses and income levels was the Chainbridge model, provided by JFO. However, because the dividing points in income categories in those results did not fit my needs, I had to estimate the numbers of filers in the different income categories that I wanted. So the intent here is to illustrate what might be possible to do with the funds available, in no way is this an accurate representation of what would actually be . *****

EXAMPLE: Vermont Standard Credit Plus $$$ for additional Housing Credit?
STANDARD TAX CREDIT PLUS HOUSING CREDIT FOR LOW AND MIDDLE INCOME LEVELS.

Totals for Different Filing Statuses for Basic VRTC 321,000 filers all statuses
[376,000 including nonresident filers]

Every Vermont resident filer at all income levels would get the standard credit. Up to certain income levels an additional housing credit would be provided.

There is some extrapolation or "guesstimation" in dividing the filers into income tiers as the divisions in the available data did not line up with the divisions that I chose for my purposes. But this shows what might be possible, depending on how the numbers of filers in the different categories line up. Remember that all additional Vermont specific adjustments to tax liability are still in place – for instance, the earned income tax credit and so forth.

	Income Up To <	VSTC	+	VHTC	=	Total VTCs	# filers	Total Cost
Single	**$25,000**	**$300**		**$488**		**$788**	**90,365**	**$71,195,620**
Married Filing Jointly	**$50,000**	**$600**		**$975**		**$1,575**	**36,019**	**$56,726,775**

Married Filing Separately	**$25,000**	**$300**	**$488**	**$788**	**1,743**	**$1,363,484**
Head of Household	**$37,500**	**$450**	**$630**	**$1,080**	**16,715**	**$18,052,200**
Totals					**144,842**	**$147,338,079**

[Credits Refundable at this level]

	Income	VSTC +	VHTC =	Total VTCs	# filers	Total Cost
S	**$25,000 -- $50,000**	**$300**	**$275**	**$575**	**47,838**	**$27,506,850**
MFJ	**$50,000 -- $100,000**	**$600**	**$550**	**$1,150**	**46,417**	**$53,379,550**
MFS	**$25,000 -- $50,000**	**$300**	**$275**	**$575**	**2,030**	**$1,167,250**
HH	**$37,500 -- $75,000**	**$450**	**$412**	**$862**	**7,716**	**$6,651,192**
Totals					**107,001**	**$88,704,842**

Total Both Income Levels: $236,042,921.

Above these income levels all filers would just get the basic VRTC with no added VRHTC:

	Income	VSTC only	# filers	Total Cost
S	**over $50,000**	**$300**	**28,030**	**$8,409,000**
MFJ	**over $100,000**	**$600**	**41,451**	**$24,870,600**
MFS	**over $50,000**	**$300**	**1,436**	**$380,800**
HH	**over $75,000**	**$450**	**3,046**	**$1,370,700**
			73,963	**$35,031,100**

Total All Income Levels: $236,042,921 + $35,031,100 = $271,074,021 < $275,000,000 funds available.

However, I don't think that the housing credit is big enough to replace Income Sensitivity property tax assistance for many participants, and I wonder whether the amount of the Standard Credit could be larger. Clearly the amount of the Standard Credit does not come anywhere close to replacing the Itemized Deductions for many filers, since many deduct thousands of dollars thus reducing tax obligations significantly after those deductions are multi

About 120,000 in Income Sensitivity Program (assuming Circuit Breaker recipients also counted in that total) About 320,000 Vermont Resident Filers all statuses, Homestead parcels around 167,025, minus around 120,000, leaves around 47,000 homestead homeowners not in Income Sensitivity. There would therefore be around 164,000 renters. (Property Valuation Review Annual Report)

The larger credit at the lower income level is important in order to replace the standard deductions and the income sensitivity property tax adjustment. But it is also important at the middle income level because the income sensitivity program went to households up to around $130,000 or so. All property tax payers will benefit from the overall reduction in taxes, to the extent that some previously in Income Sensitivity would no longer have qualified at the lower tax payments.

At upper income levels the Vermont credit will only partially replace the itemized deductions lost. But those with upper income levels that own property will benefit from the property tax reduction.

It might still be necessary to continue the Circuit Breaker program that provides extra support to Vermonters whose combined municipal and education property taxes exceed a certain percentage of their income.

It might be possible to provide that the Homeowner Credit could be sent directly to Towns to pay education property taxes, either on the tax form or as a voucher.

Based on my calculations given the data that I have about the numbers of returns that there are in these different filing categories and income levels, the $275 million tax reform dividend should be enough to cover these tax credits.

An alternative approach would be to use the $275 million "tax reform dividend" for a refundable tax credit at the lower income levels, but then use the remaining funds to reduce tax rates instead of to provide a tax credit to all filers. Reducing rates at the lowest levels doesn't seem useful since reducing a rate on a low level of income will result in a small reduction of tax liability. But it might be possible to take the tax dividend funds remaining after the low income tax credit and use it to reduce the rates in such a way that tax liability in each bracket is reduced by the same dollar amount. I think that the best way to do this would be to reduce the rates in the second tax bracket in this way, and then all taxpayers at that and at upper levels would have their tax liability reduced by the same DOLLAR amount of $300 or $600, respectively.

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RESULTS:

These examples show that ---

*** the broadening of the tax base through eliminating federal pass through deductions and including the value of employer provided benefits in income can provide the funding to allocate a standard tax credit to all taxpayers and then target particular income levels for additional support;

*** it is therefore possible to improve the horizontal and vertical equity of the system;

*** it might be possible to provide for a housing credit within the income tax system instead of within the Education Fund, although it may be necessary to continue the Circuit Breaker program for some Vermonters – this housing credit is a way to target assistance at the income levels most challenged in obtaining affordable housing, rather than allocating a variety of amounts to higher income levels through the Mortgage Interest deduction, the Real Estate deduction, and the upper levels Income Sensitivity eligibility;

*** it might therefore be possible to make progress towards achieving policy goals connected to affordable housing for renters as well as homeowners at the low to middle income levels;

*** it might be possible to make both the income tax system and the property tax system simpler and more accountable.

It terms of the effects on different types of taxpayers ---

Those who had taken itemized deductions – how much their income tax liability would go up in this approach would depend on how much they took and what tax bracket they were in – for those who also own property those taxes will decline – if the net effect for a taxpayer is that tax liability increases when all netted out, they I have to wonder if they were paying a reasonable share before. All the itemized deductions continue to be available at the level of Federal Income Taxation until and unless removed under the tax change legislation currently under consideration in Washington. [This situation has clearly been affected by the legislation actually passed since this paper was drafted early in 2017.]

Those who have employer provided benefits – such taxpayers will have higher incomes and therefore potentially higher tax liability, but the size of the increase depends on the tax bracket they are in, and if they are in the lower income levels lower liability may be offset by the new tax credits; also the decline in property taxes may offset some of this.

For those at the lower income level, remember that this analysis is only about changing the Federal itemized deductions and including the benefits – the Vermont Earned Income Tax Credit and other provisions remain in effect. As stated above, it may be necessary to continue a version of the Circuit Breaker program for those with very low incomes. In addition, it would be important to ascertain how these refundable tax credits would be viewed within the eligibility frameworks for Federal benefits in order to avoid creating some kind of unintended benefits cliff or penalty.

This approach of giving the standard credit instead of a standard deduction provides the same reduction in tax liability for all income levels. In the standard deduction approach the value of the deduction is greater at higher tax bracket levels if one thinks of the income being reduced at the highest level that a taxpayer's income reach. And of course many taxpayers use the itemized deductions to reduce their obligation by way more than the amount of the standard deduction within the limits currently in place in the Vermont code.