

An Overview of the Final Report of Vermont's Blue Ribbon Tax Structure Commission

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The origins of the report

- Prepared in accordance with Act 1, Sec. H. 56 of the 2009 Special Legislative Session
- Commission members
 - Kathleen C. Hoyt
 - William R. Sayre
 - Bill Schubart
 - Michael Costa, Director (Principal Researcher)

The purpose and goals

- “The commission shall prepare a structural analysis of the state’s revenue system and **offer recommendations** for improvements and modernization and **provide a long-term vision for the tax structure.**”
- “The commission shall have as its goal a tax system that provides **sustainability, appropriateness, and equity.**”

Principles, unanimously agreed upon, that guided the Commission's work

- Fairness, Actual and Perceived
 - Impose similar burdens on people in similar circumstances, minimize regressivity, and minimize taxes on low-income people
 - Touchstones: broad base and low rate, progressive, ubiquitous
- Economic Competitiveness
- Simplicity
 - Ease of compliance, ease of administration,
- Transparency
- Tax Neutrality
 - Raise needed revenue without micromanaging the economy
- Sustainability
 - Produce predictable and consistent revenue
- Executive and Legislative Accountability to Tax Payers
- Revenue Neutrality and Interoperability

The Commission's Findings

Six findings that address common misperceptions about Vermont's tax system

1. The Vast Majority of Vermonters Pay Taxes.

- Vermont's tax system has a remarkably even distribution if one considers income, sales, and property taxes. Claims that some Vermonters do not pay their fair share are typically based on personal income tax distribution and ignore other taxes and rising income inequality.

2. Vermont's Choice of Income Tax Base Promotes High Marginal Rates and Lower Effective Rates.

- Vermont's choice of tax base (based on federal taxable income) makes tax rates unnecessarily high as federal deductions pass through and reduce taxable income. The effective tax rates paid by Vermonters are competitive with other states.

3. Changing Consumer Buying Patterns are Eroding Vermont's Sales Tax Base and Should be the Focus of Policymakers.

- Rising purchases of services over goods and growing Internet sales are eroding Vermont's sales tax base.

Findings, continued

4. Tax Expenditures Form a Shadow Budget that Requires Greater Scrutiny.

- The tax system loses over \$1 billion annually due to insufficient oversight. Tax expenditures are policy choices made within the tax system, and they lack sufficient transparency.

5. There is Insufficient Data to Claim that Vermonters are Migrating Due to High Taxes – Current Statistics Demonstrate an In-Migration of Income.

- Available data suggests that those entering Vermont earn more than those leaving. Also, Vermont's top tax bracket is populated by high-income events, not high-income earners. While the data cannot determine something as subjective as why people are moving, it does demonstrate that definitive claims that the wealthy are moving out and about the effect of this migration are more complicated than currently assumed.

6. The Complexity of Vermont's Education Funding System Obscures Basic, if Difficult, Tax Structure Issues.

- The mechanics of the tax are complex, but the basic tax structure tension is rooted in equity. This manifests itself in the discussion regarding what is the “right” tax to fund education. Transition toward a tax system rooted more in property value or income would trigger a tax shift that puts pressure on the tax principles of equity and competitiveness.

The Commission's Recommendations

RECOMMENDATION 1: RESTRUCTURE THE PERSONAL INCOME TAX

- 1A: Shift tax base from federal Taxable Income to federal Adjusted Gross Income.
- 1B: Eliminate standardized and itemized deductions.
- 1C: Implement a lower, flatter rate and bracket structure.
- 1D: Implement a residential credit as a transparent alternative to deductions.
- 1E: Evaluate all remaining personal income tax expenditures for opportunities for removal.
- 1F: Reduce the number of filing statuses from four to two, single and joint.

RECOMMENDATION 2: BROADEN THE SALES TAX BASE

- 2A: Levy the general sales tax on all consumer-purchased services with limited exceptions for certain health and education services and business-to-business service transactions.
- 2B: Eliminate all consumer-based sales tax expenditures retaining only the exemptions for food and prescription drugs.
- 2C: Cut the sales tax rate from 6 percent to 4.5 percent.
- 2D: Move as aggressively as possible with other states to collect tax revenue due on Internet purchases.
- 2E: Levy the sales tax on soda by removing its tax exemption as a food product.

RECOMMENDATION 3:

ENHANCE SCRUTINY OF TAX EXPENDITURES

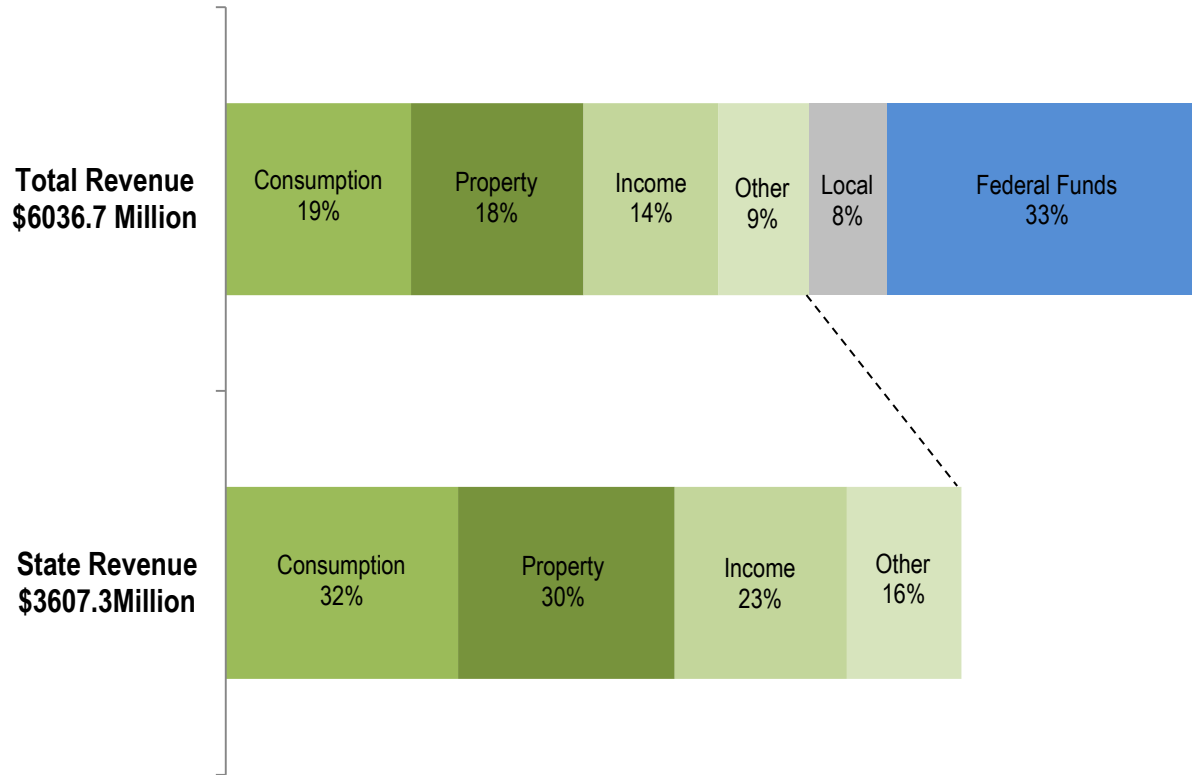
- 3A: Develop a legislative intent for each tax expenditure.
- 3B: Report the foregone revenue value of each tax expenditure biennially in the tax expenditure budget and refine the capacity to evaluate these values.
- 3C: Sunset all tax expenditures that remain in the tax code in a multi-year cycle so that the Legislature evaluates and affirms these policy choices and require a sunset for new tax expenditures as a matter of good, transparent public policy.
- 3D: Require an evaluation of the valuation of tax exempt properties on the grand list, particularly those that qualify for the public, pious, and charitable exemption from the property tax. Any such mandate ought to be accompanied by a sufficient appropriation from the Legislature to avoid levying an unfunded mandate on local officials.

RECOMMENDATION 4: INVEST IN TAX POLICY RESOURCES

- 4A: Develop or use a tax incidence study so that the Legislature may understand the full ramifications of its tax policy choices.

Balance across Revenue Sources:

Fig. 7. Total Vermont Revenue and State Revenue, FY 2015



Recent information from the 2017 10-Year Tax Study, JFO

- <http://www.leg.state.vt.us/jfo/reports/2017%2010%20Year%20Tax%20Study%20Full%20Report%20Compressed.pdf>

Figure 12. Income Tax Revenue and Percentage of Total Tax Paid by Decile of Resident Tax Filers, Tax Year 2015

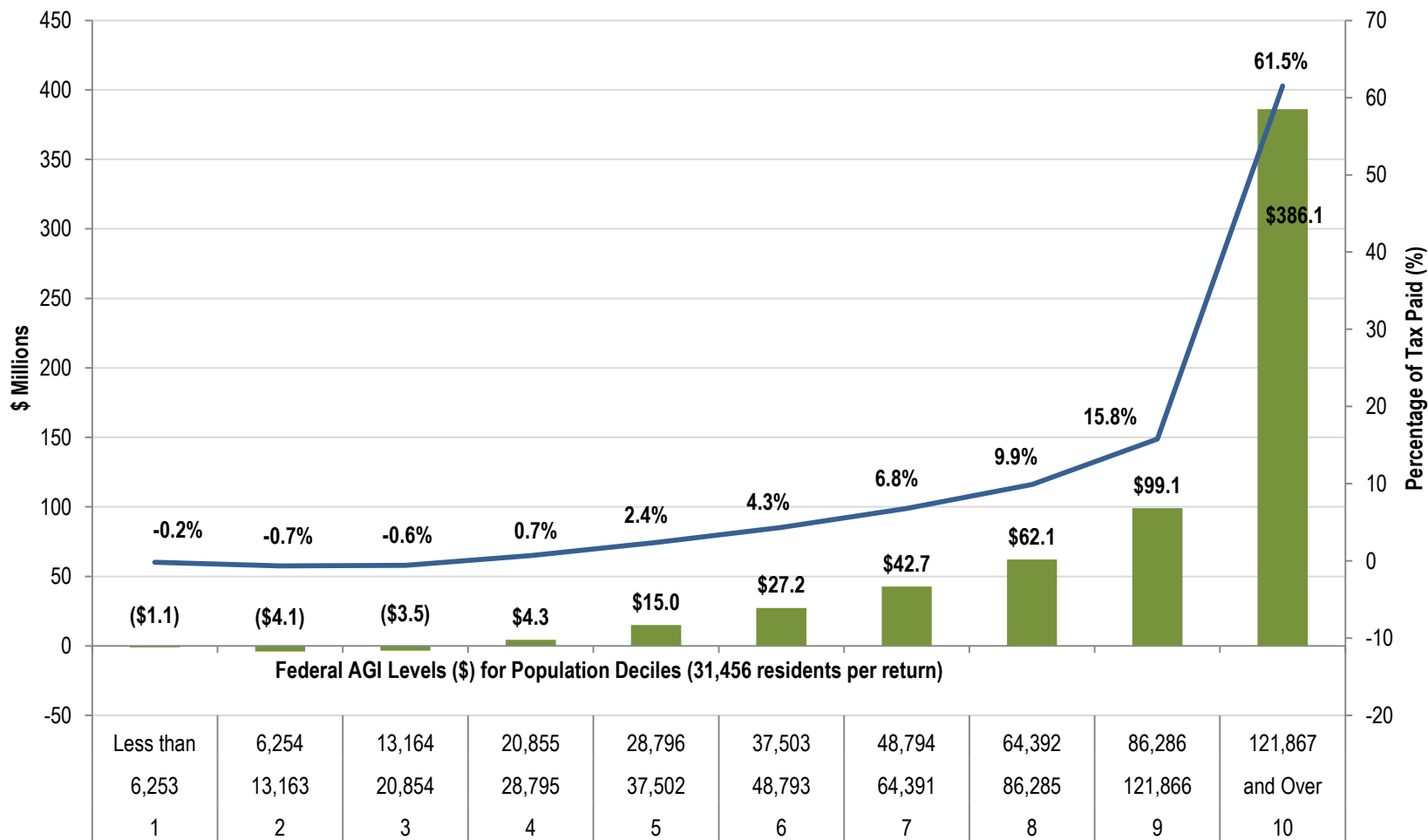
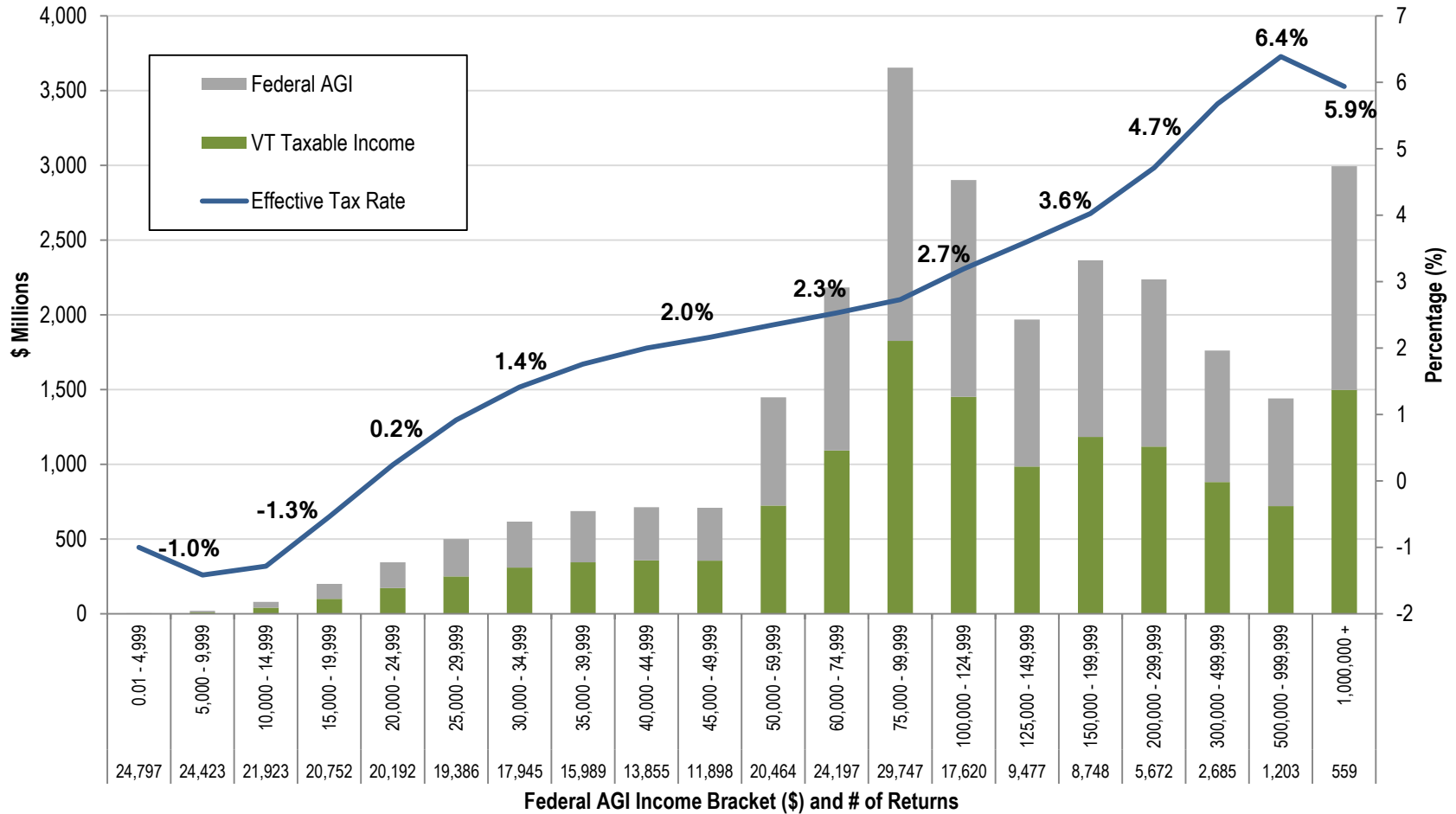


Fig. 14. Effective Tax Rates and VT Taxable Income as a Share of Federal AGI, Tax Year 2014



Note: Vermont's average effective tax rate in 2014 was 3.2 percent.

Fig. 17. Migration of Vermont Resident High-Income Tax Filers, CY 2005-2014

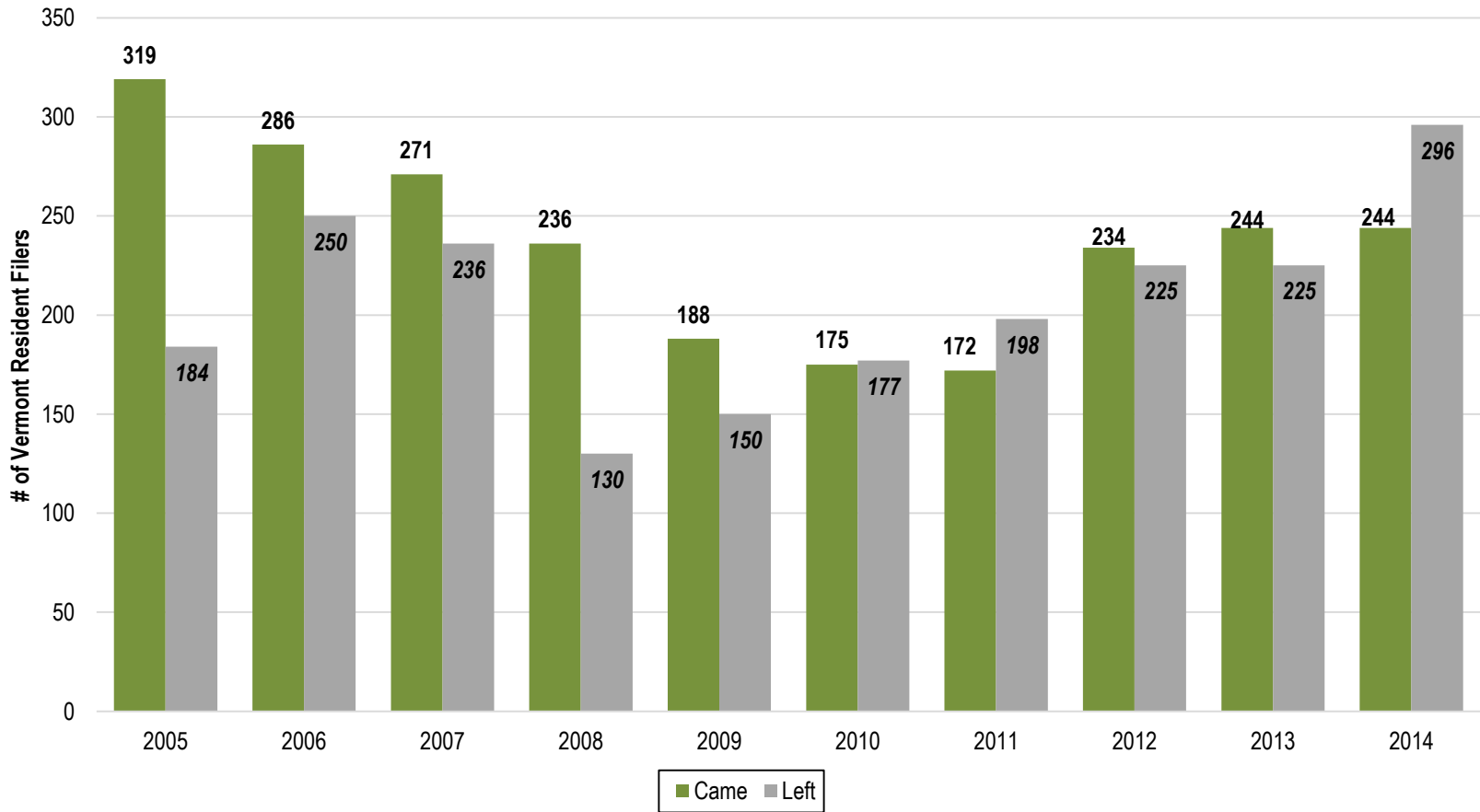
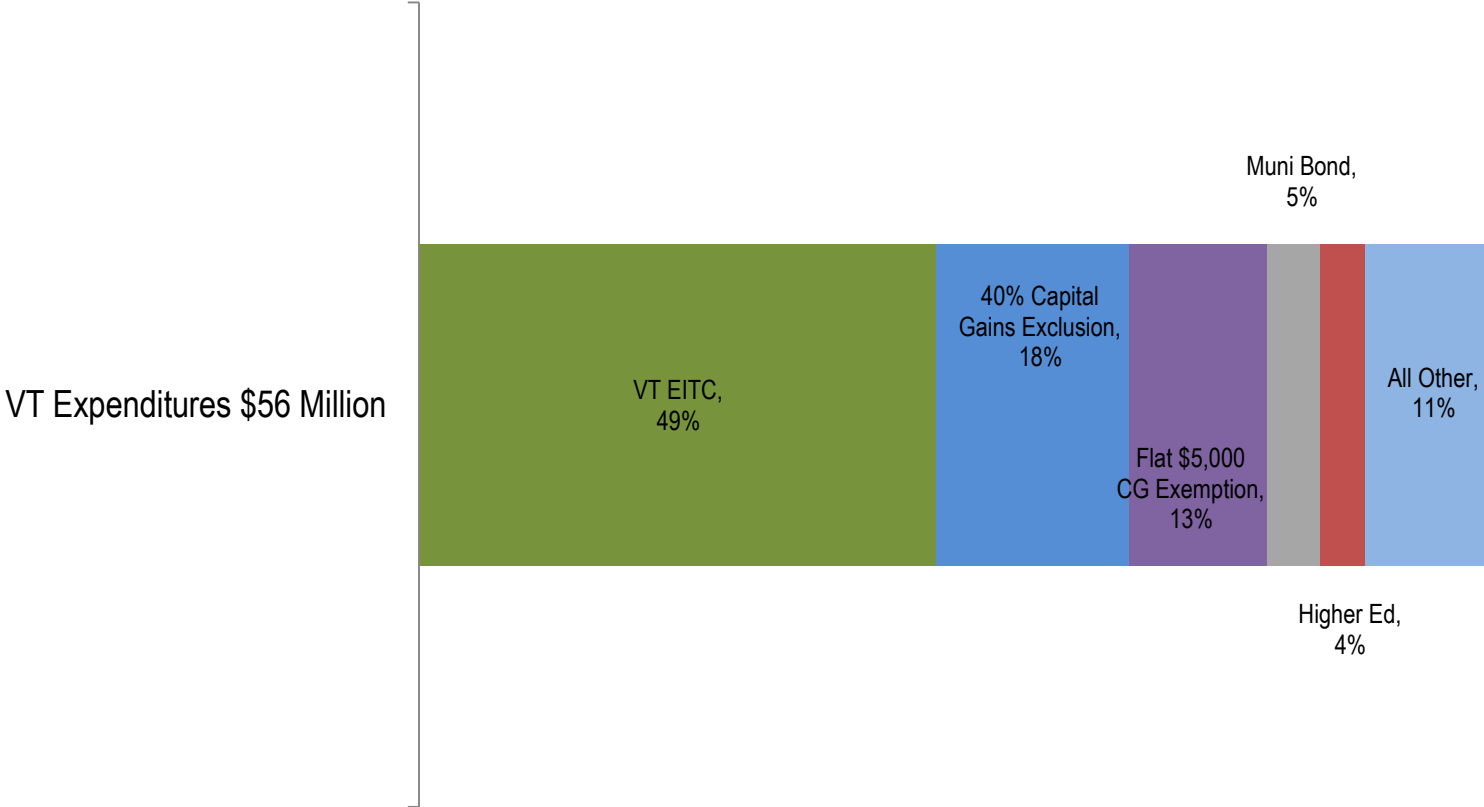


Fig. 19. Vermont Individual Income Tax Expenditures by Value, FY 2015



AGI vs. Taxable Income

- Total Income
 - Less deductions for
 - Health insurance, IRA/401k/HSA contributions, alimony paid, tuition and fees, job-related moving expenses, part of the self-employment tax, educator expenses, student loan interest
- Equals AGI (Adjusted gross income)
 - Less personal exemptions and standard or itemized deductions
 - State and local taxes paid, mortgage interest, charitable contributions, job expenses, medical expenses
- Equals Federal Taxable Income

Federal vs. Vermont Taxable Income

- Federal taxable income
 - Plus
 - Interest and dividend income from non-Vermont state and local obligations
 - Bonus depreciation allowed under federal law depreciation
 - State and local income tax addback
 - Minus
 - Interest income from U.S. obligations
 - Capital gains exclusion
 - Flat exclusion (capital gains)
 - Percentage exclusion (40% of adjusted net capital gains if held more than 3 years)
 - Adjustment for bonus depreciation on prior year property
- Equals Vermont taxable income

AGI, Federal and Vermont taxable income, 2007 and 2015

	Residents	Residents	Residents	Non-residents	
	2007 -- report	2007 -- online	2015	2015	
Total income	\$15.3 bil				
AGI	\$15 bil	\$16.7 bil	\$18.9 bil	\$7.2 bil	
Fed taxable income	\$10.2 bil	\$11.6 bil	\$13.2 bil	\$6.0 bil	
VT taxable income		\$10.9 bil	\$13.6 bil	\$6.4 bil	
2011 report:					

Vermont is one of only nine states to define income as federal Taxable Income and shrink its tax base by adopting all federal deductions and exemptions.¹³ Twenty-seven states define income as Adjusted Gross Income, including all other New England states and New York. ¹⁴ The choice to define income as Adjusted Gross Income by the majority of states, including Vermont's nearest neighbors, means that these states create a much larger personal income tax base.

Fig. 26. Consumption Taxes in Vermont, FY 2015

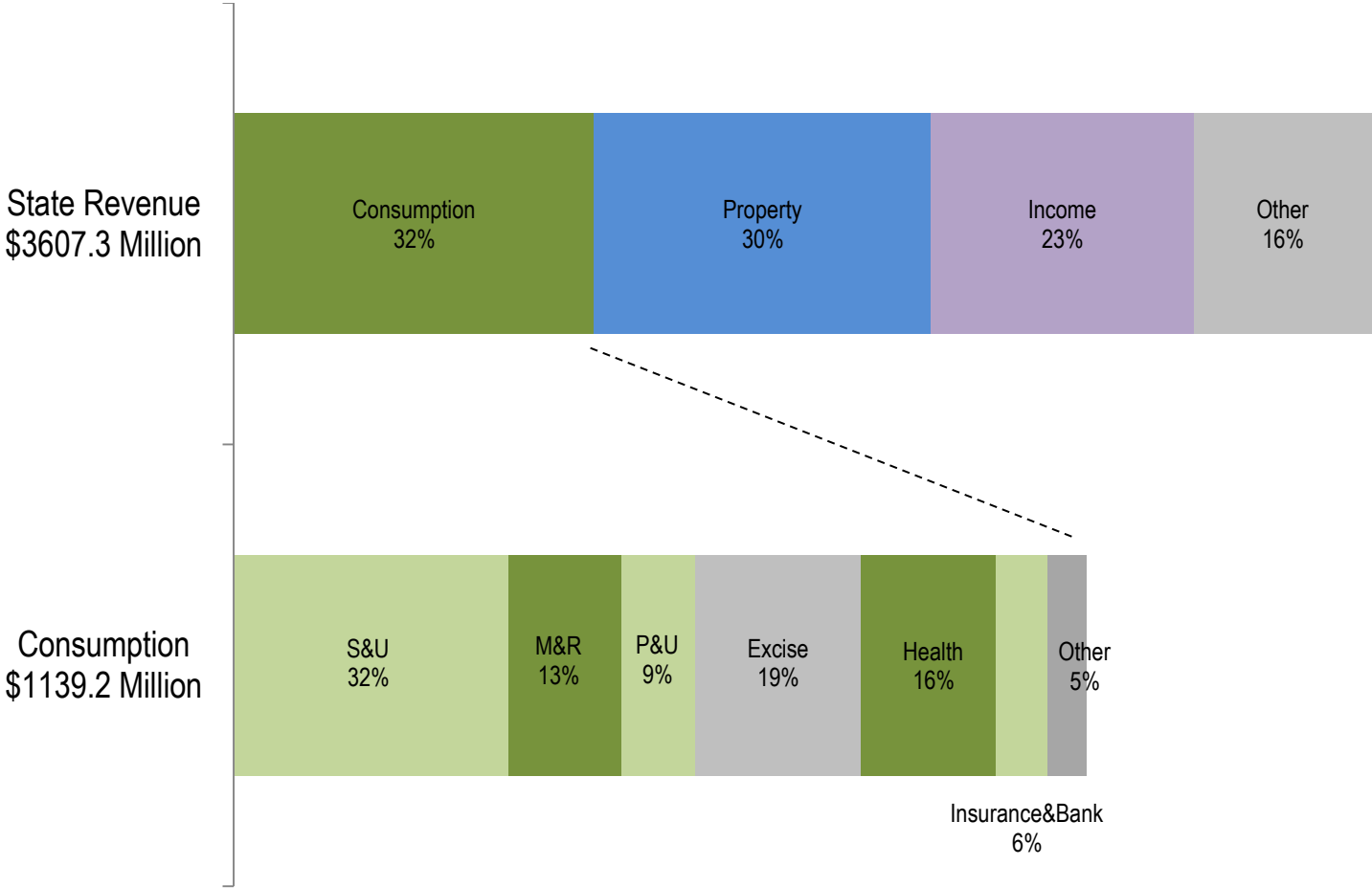


Table 31. Share of After-Tax Income in the U.S. Spent on Consumption Categories by Age Group, 2014

Household Income	<25	25-34	35-44	45-54	55-64	65+
Income after taxes	\$28,986	\$56,052	\$72,891	\$77,125	\$63,815	\$42,509
Shares of after-tax income spent (%)						
Food away from home	7.3	5.4	5.0	4.6	4.3	4.9
Alcoholic beverages	1.0	1.0	0.7	0.7	0.8	1.3
Owned dwellings	3.9	7.6	10.6	10.8	10.8	12.9
Utilities, fuels, and public services	6.9	5.9	5.9	6.0	6.7	8.6
Vehicle purchases (net outlay)	9.7	7.3	5.9	5.9	5.6	5.7
Gasoline and motor oil	5.4	4.1	3.8	3.7	3.7	3.8
Healthcare	3.6	4.9	5.4	5.9	7.9	13.6
Tobacco products and smoking supplies	0.8	0.6	0.5	0.6	0.6	0.5
Life and other personal insurance	0.1	0.2	0.4	0.6	0.8	0.8

Fig. 36. Property-Based Taxes in Vermont, 2015

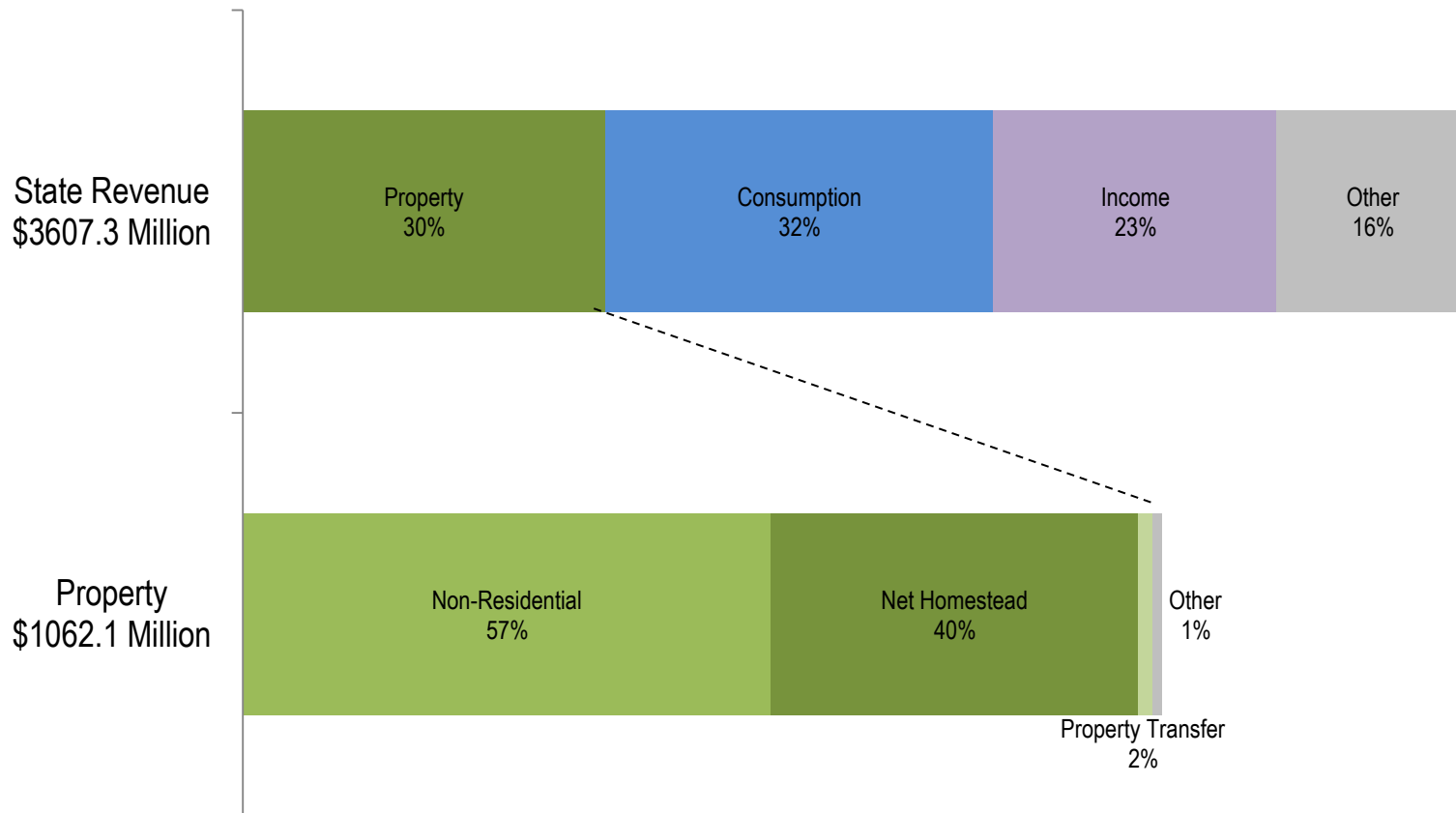


Fig. 37. Education Property Tax Paid, FY 2015



Fig. 39. Education Tax as a Percentage of Household Income, CY 2015

