

# Vermont Legislative Joint Fiscal Office

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## Draft ISSUE BRIEF

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### Education Finance Issues Raised by the COVID-19 Pandemic

#### Summary

- Non-property tax revenues dedicated to the Education Fund (EF) in FY2020 are now expected to fall \$35 to \$45 million below the January forecast.
- Municipalities have already collected most of the education property taxes due in FY2020; however, 74 municipalities still have an estimated \$125 million outstanding.
- School districts will need to reallocate existing funds, use reserves, or run deficits to cover the cost of any COVID-19 related spending in the 2019-2020 school year.
- School districts receive three equal payments from the EF. The last payment, due on April 30<sup>th</sup>, is still outstanding.
- Businesses will be allowed to defer transfer of some trustee taxes due in March and April to May 25<sup>th</sup>; even if this revenue is fully remitted by the end of this fiscal year, this deferral may create an EF cash flow problem in FY2020.
- The EF will run a significant operating deficit in FY2020 – the projected \$12.9 surplus and the most of the projected \$36.4 million stabilization reserve will be depleted.
- The Federal COVID-19 stimulus package includes \$13.5 billion for elementary and secondary schools. Vermont's share of this additional school aid should be available in the current fiscal year for distribution to school districts.
- Setting the education tax rate parameters for FY2021 prior to adjournment will be problematic given the current level of uncertainty. However, if these parameters are not set prior to adjournment, there are default parameters set forth in current law.
- COVID-19 related EF revenue losses are expected to be significantly higher in FY2021 for both education property taxes and non-property taxes; however, reliable estimates are not yet available.
- Voters have already approved 94 school budgets that will increase education spending by \$73 million over FY2020 levels in FY2021.
- Voters defeated nine school budgets in March and other school districts have votes scheduled in April or May. How and when these votes will take place now is uncertain.
- The property tax credit for FY2021 will be based on CY2019 income, so there will be no additional property tax assistance for taxpayers with COVID-19 related loss of income.
- Moving the filing deadline for the property tax credit to July 15<sup>th</sup> creates a potential problem for municipalities to issue timely education property tax bills in FY2021.

### **COVID-19 Related Loss of Education Fund Revenue FY2020**

In the January revenue forecast, total EF sources were estimated to be nearly \$1,711 million. Of this amount, education property taxes accounted for \$1,140 million or roughly two-thirds of total EF revenue. Non-property taxes accounted for the remaining \$528 million, or roughly one-third of total EF revenue.

Most of the education property taxes due for the current fiscal year have already been collected by municipalities. However, each municipality has its own billing schedule and at present many municipalities still have outstanding tax payments due. How much of these outstanding taxes will not be paid in a timely fashion due to COVID-19 related layoffs or business losses is uncertain.

Number of Payments	Number of Towns	Net Education Property Taxes Collected (\$M)	Towns with Payments Due	Net Education Property Taxes Due (\$M)
1	108	\$288	0	\$0
2	62	\$251	21	\$32
3	19	\$192	8	\$16
4	45	\$229	45	\$76
No data	25	\$58	-	-
<b>Total</b>	<b>259</b>	<b>\$1,018</b>	<b>74</b>	<b>\$125</b>
<i>Percent of Total</i>	-	89%	-	11%

As indicated in this table, there are currently 74 municipalities that have \$125 million in outstanding education property tax collections for FY2020 as of March 15<sup>th</sup>. The statewide cost of failure to collect one-percent of these outstanding property taxes would be only \$1.25 million. However, there are 21 municipalities that have not yet collected one-half of their total education property tax collections.

Non-property tax revenues from the sale and use, purchase and use, and meals and rooms taxes were estimated to raise almost \$528 million in FY2020. Total revenues from these three non-property taxes are now expected to fall \$35 to \$45 million below the January revenue forecast as the economy slows due to layoffs and business losses and consumers reign in their discretionary spending. This loss represents about 2% to 2.6% of total EF revenues in FY2020.

In addition, the Administration will allow businesses to defer payment of the sales and use tax and the meals and rooms taxes due in March and April to May 25<sup>th</sup>. If businesses are able to remit the total amount of outstanding tax due on May 25<sup>th</sup>, this will not result in an additional revenue downgrade for FY2020; however, collection of the full amount due after deferral is not a certainty. Even if remitted in full, this trustee tax deferral may create a cash flow issue for the EF in the current fiscal year.

## **COVID19-Related Spending by School Districts in FY2020**

In response to the COVID-19 pandemic, the Governor ordered the dismissal of all schools and the cancellation of all school-related activities through April 6<sup>th</sup>. During this period of dismissal, school employees are directed to report to work or to work remotely and school districts have been directed to continue to pay all school staff, including hourly employees, and to continue to make prekindergarten tuition payments to private providers.

Although guidance from the Agency of Education (AOE) indicates that during the initial dismissal period, regular educational services do not continue and students are not expected to make educational progress, other services will continue to be supported by school employees including:

- *District-based options for childcare for “essential” employees*
- *Meals services for those who need it*
- *Creating a plan for continuing services for students with disabilities and special needs*
- *Systems for ensuring the maintenance of education for students*
- *Cleaning and disinfecting school grounds*

The additional cost associated with the provision of these services may not be large. School districts remain eligible for certain Federal and State reimbursements for school meals and the Administration has indicated that school districts that require supplemental funding for child care services provided to essential workers will also be reimbursed, although the source and amount of this funding is uncertain.

If, as now seems likely, it becomes necessary to extend closure period beyond April 6<sup>th</sup>, school districts will be asked to provide more formal education services to students for the remainder of the school year. Schools will be required to create Continuing Education Plans for all students and all educational services, to the extent possible, must be offered to students through various remote and virtual means.

Since school budgets are set, any additional funding required to provide educational services during the 2019-2020 school year will require school districts to reallocate existing funds, use reserve funds, if available, or run a deficit that would carryforward into the next school year. However, this far into the current school year school districts have less flexibility to reallocate funds and districts are universally thin on reserves.

## **Cash Flow Issues in FY2020**

Prior to the COVID-19 outbreak, the EF was projected to close FY2020 with a full stabilization reserve of \$36.4 million and a surplus of \$12.9 million. This surplus will reduce a portion of the anticipated \$35 to \$45 million revenue shortfall. However, without additional funding from some other source such as the pending Federal COVID-19 stimulus bill, the EF will run a significant operating deficit in FY2020 and most of the stabilization reserve will be needed to cover statewide education spending.

Under current law, school districts receive three equal payments from the EF on September 10<sup>th</sup>, December 10<sup>th</sup>, and April 30<sup>th</sup>. For school year 2019-2020, the April 30<sup>th</sup> payment to school

districts is still outstanding. This payment includes state categorical aid for special education, transportation, and small schools as well as the education payment. Revenue losses and deferral of some trustee taxes could create a cash flow issue for the EF.

Municipalities must be timely in their payments of statewide education property tax to the State even if property taxpayers are delinquent or fail to pay their taxes. Consequently, in addition to losing municipal property tax revenue, municipalities would need to remit the full amount of education property tax owed to the State. There is also an 8% penalty for late payments, but the Commissioner of Taxes likely can exercise his general authority to waive the penalty.

### **Federal COVID-19 Stimulus Bill**

The Federal COVID-19 stimulus bill includes \$13.5 billion for formula grants to states. States must distribute 90% of their allocation to school districts based on their proportional allocation of Elementary and Secondary Education Act I-A funds. Up to 10% of the allocation may be retained for emergency needs.

Funds distributed to school districts may be used for CORONA-19 response activities, such as planning for and coordinating during long-term school closures; purchasing educational technology to support online learning; and additional activities authorized by federal elementary and secondary education laws.

### **Setting Education Tax Rates for FY2021**

Prior to adjournment, the Legislature normally sets the property and income yields as well as the nonhomestead property tax rates for the upcoming fiscal year. Given the current level of uncertainty about the health of the EF at the close of FY2020 and the magnitude of any FY2021 revenue shortfall, setting education property tax parameters for FY2021 will be problematic.

COVID-19 related revenue losses are expected to be significantly higher in FY2021 than they are in FY2020. At this point in time reliable estimates of how significant those revenue losses will be are not available. The Legislative economist is current assessing likely FY2021 revenue impacts in the light of evolving epidemiological models; however, it is not clear given current uncertainties when reliable revenue estimates will be available for FY2021.

Voter-approved EF spending for FY2021 is \$73 million higher than in FY2020. In March voters approved 94 school district budgets that increased education spending by \$62 million over FY2020 levels. Other EF spending for State categorical aid as well as other uses is estimated to be up another \$11 million over FY2020 levels. Note that any reduction in State categorical aid for special education, transportation, or small schools will increase education spending by the same amount.

Even if it is possible to undue voter-approved education spending, efforts by districts to reduce budgeted education spending in FY2021 would be constrained by existing teacher contracts since salaries and benefits alone account for almost 80% of education spending statewide. In districts with contracts in place for FY2021, the only way to significantly reduced spending

would be to lay off teachers and other staff – an undesirable outcome if the midst of an economic downturn.

In March voters defeated nine school district budgets and in five school districts the vote is scheduled in April or May. When the municipalities that belong to these districts will be able to vote on their school budget is uncertain. Note that if voters are unable to pass a school budget by June 30<sup>th</sup> there is a default in current law that will allow a school district to continue to operate by borrowing funds necessary to enable it to operate on a budget up to 87% of the most recently approved budget.

If the yields and nonhomestead tax rate are not set prior to adjournment, there are default parameters set forth in current law. The property and income yields would remain at their FY2020 level and the nonhomestead tax rate would remain at its statutory level of \$1.59. Alternatively, these tax rate parameters could be set as recommended by the Commissioner of Taxes last December. Board-approved school budgets were presumably presented to voters with the spending-adjusted homestead tax rates that result from these parameters in mind.

	FY2020	FY2021 – December	FY2021 – Defaults
Property Yield	\$10,648	\$10,883	\$10,648
Income Yield	\$13,081	\$13,396	\$13,081
Uniform Nonhomestead Tax Rate	\$1.594	\$1.654	\$1.590
Average Homestead Tax Rate	\$1.510	\$1.558	\$1.593
Average Income Tax Rate	2.47%	2.55%	2.60%
<b>Estimated Revenue (\$M)</b>	<b>\$1,140</b>	<b>\$1,220</b>	<b>\$1,206</b>
Net Homestead Taxes	\$447	\$476	\$490
Nonhomestead Taxes	\$694	\$744	\$716

### Other Issues

The property tax credit for FY2021 (fall 2020) will be based on CY2019 household income filed in April-July. Consequently, there will no additional property tax assistance for taxpayers who lose income due to COVID-19 related layoffs or business losses until FY2022 (fall 2021). In FY2022 (fall 2021), the property tax credit is likely to increase significantly.

Under current law, the filing deadline for both the homestead declaration and the property tax credit claim is April 15<sup>th</sup>. The Commissioner of Taxes has now pushed that deadline back to July 15<sup>th</sup> to conform with the personal income tax filing deadline. This creates a potential problem for municipalities to issue timely net education property tax bills in FY2021.