

Introduction to Vermont's Education Finance System

JANUARY 2020



Vermont Legislative
JOINT FISCAL OFFICE

OVERVIEW

In this presentation we are going to go over the following components of Education Finance in Vermont:

1. Review property tax timelines
2. The Education Fund Outlook and revenues available to support education expenditures
3. Key education terminology and how homestead property taxes are calculated
4. An introduction to the property tax credit

EDUCATION FINANCE TIMELINE

1. On or before December 1st, the Tax Commissioner projects education tax rates for the next fiscal year.
2. School boards develop budgets and submit them to voters for their approval in March at town meeting or by Australian Ballot.
3. The Legislature sets the yields and base education tax rates at the level necessary to fund voter-approved school budgets before adjournment.
4. The Tax Department sets spending-adjusted homestead tax rate for each town on or before June 30th.
5. Towns send tax bills to property owners on local schedules (typically in the late summer and early fall).
6. School districts receive payments from the Education Fund to fund the approved budgeted operations.

THE EDUCATION FUND OUTLOOK

The Education Fund Outlook allows legislators to:

- Determine the amount of revenue that must be raised through education taxes
- Set yields/base education tax rates
- Evaluate education finance policy changes

The following questions, addressed in the next four slides, provide a broad overview of the information included in the Outlook:

- What are the sources of EF revenue?
- How are these revenues used?

The numerical values in the following slides represent FY2019 funding.

The Education Fund Outlook is not a fund statement: uses are appropriations rather than actual expenditures and does not include unused appropriations that are designated by the Administration for continuing appropriation.

THE EDUCATION FUND OUTLOOK

| <i>(millions of dollars)</i> | FY2019 Actual | FY2020 Actual |
|---|--------------------------|--------------------------|
| a Average Homestead Property Tax Rate | \$1.499 | \$1.510 |
| b Average Tax Rate on Household Income | 2.48% | 2.47% |
| c Uniform Non-Homestead Property Tax Rate | \$1.580 | \$1.594 |
| d Property Yield Per Equalized Pupil | \$10,220 | \$10,648 |
| e Income Yield Per Equalized Pupil | \$12,380 | \$13,081 |
| f Equalized Pupil Count | 88,359 | 87,839 |

Sources

| | | |
|---|----------------|----------------|
| 1a Homestead Education Property Tax | 594.9 | 609.5 |
| 1b Property Tax Credit | (165.9) | (165.8) |
| 3 Non-Homestead Education Property Tax | 676.7 | 700.3 |
| 4 Sales & Use Tax | 412.5 | 432.5 |
| 5 Purchase & Use Tax - <i>one-third of total</i> | 37.3 | 35.1 |
| 6 Meals & Rooms Tax - <i>one-quarter of total</i> | 45.5 | 40.9 |
| 7 Lottery Transfer | 29.5 | 26.8 |
| 8 Medicaid Transfer | 11.3 | 10.6 |
| 9 Other Sources (Wind & Solar, Fund Interest) | 3.4 | 5.1 |
| 10 Total Sources | 1,645.0 | 1,695.0 |

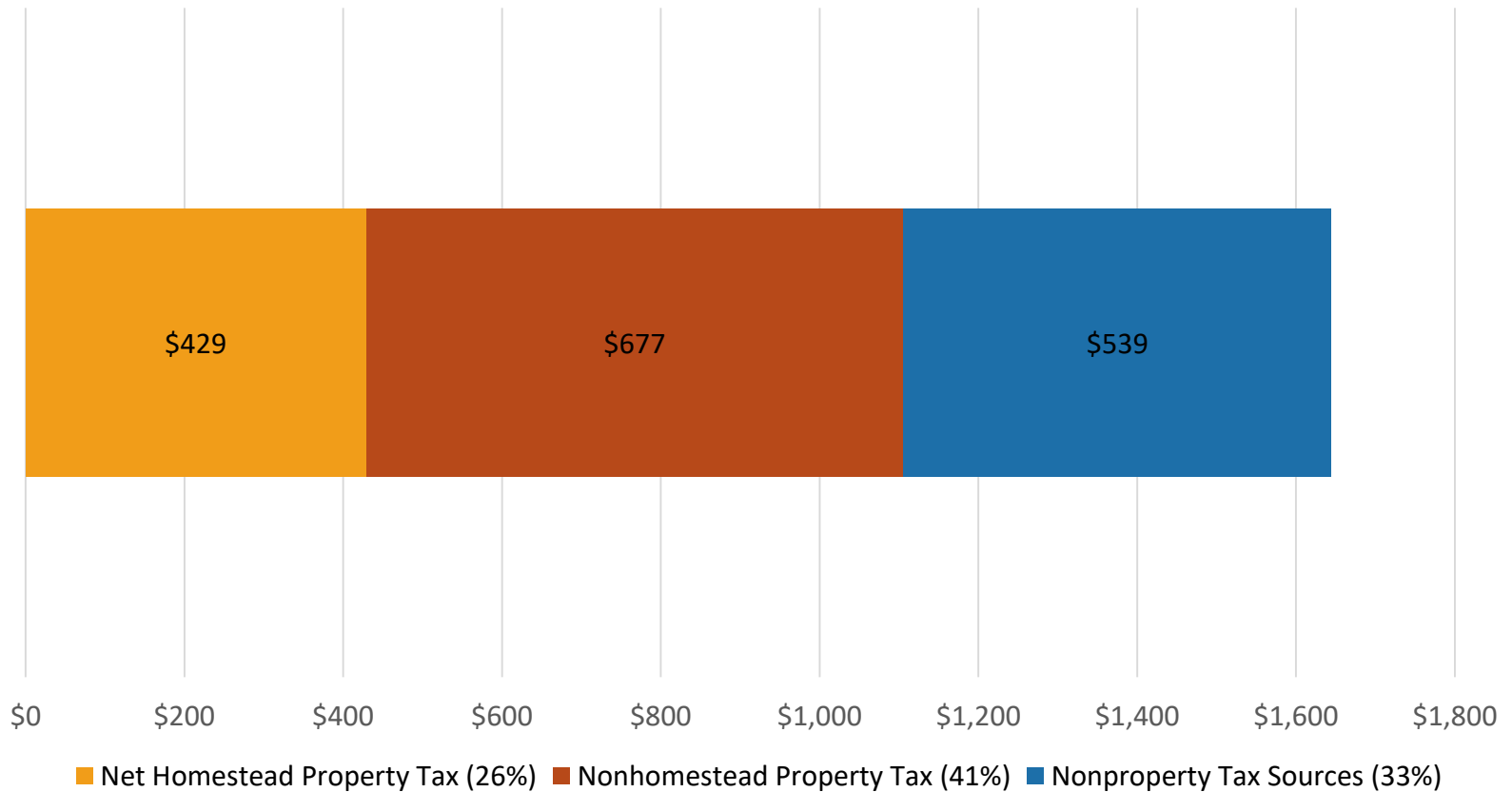
Appropriations

| | | |
|--------------------------|---------|---------|
| 11 Education Payment | 1,372.9 | 1,428.8 |
| 12 Special Education Aid | 198.5 | 213.0 |
| 13 State-Placed Students | 20.4 | 18.0 |

EDUCATION FUND SOURCES

Two-thirds of total recurring sources are raised on the education property tax.

Education Fund Sources FY19

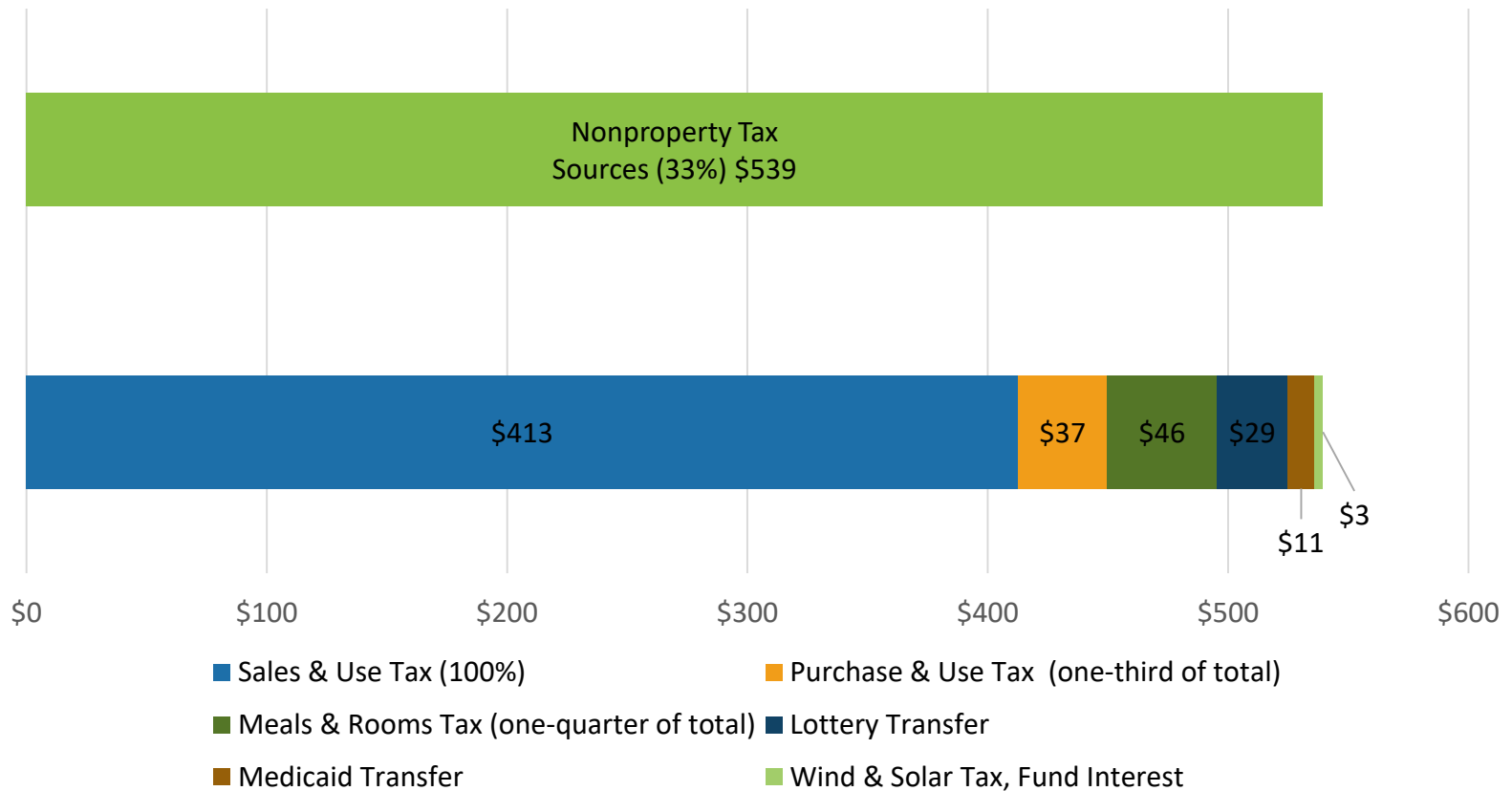


The net homestead property tax is the gross homestead property tax less the property tax credit.

NON-PROPERTY TAX SOURCES

One-third of total recurring sources are non-property tax sources.

FY19 Education Fund Nonproperty Tax Revenues (\$M)

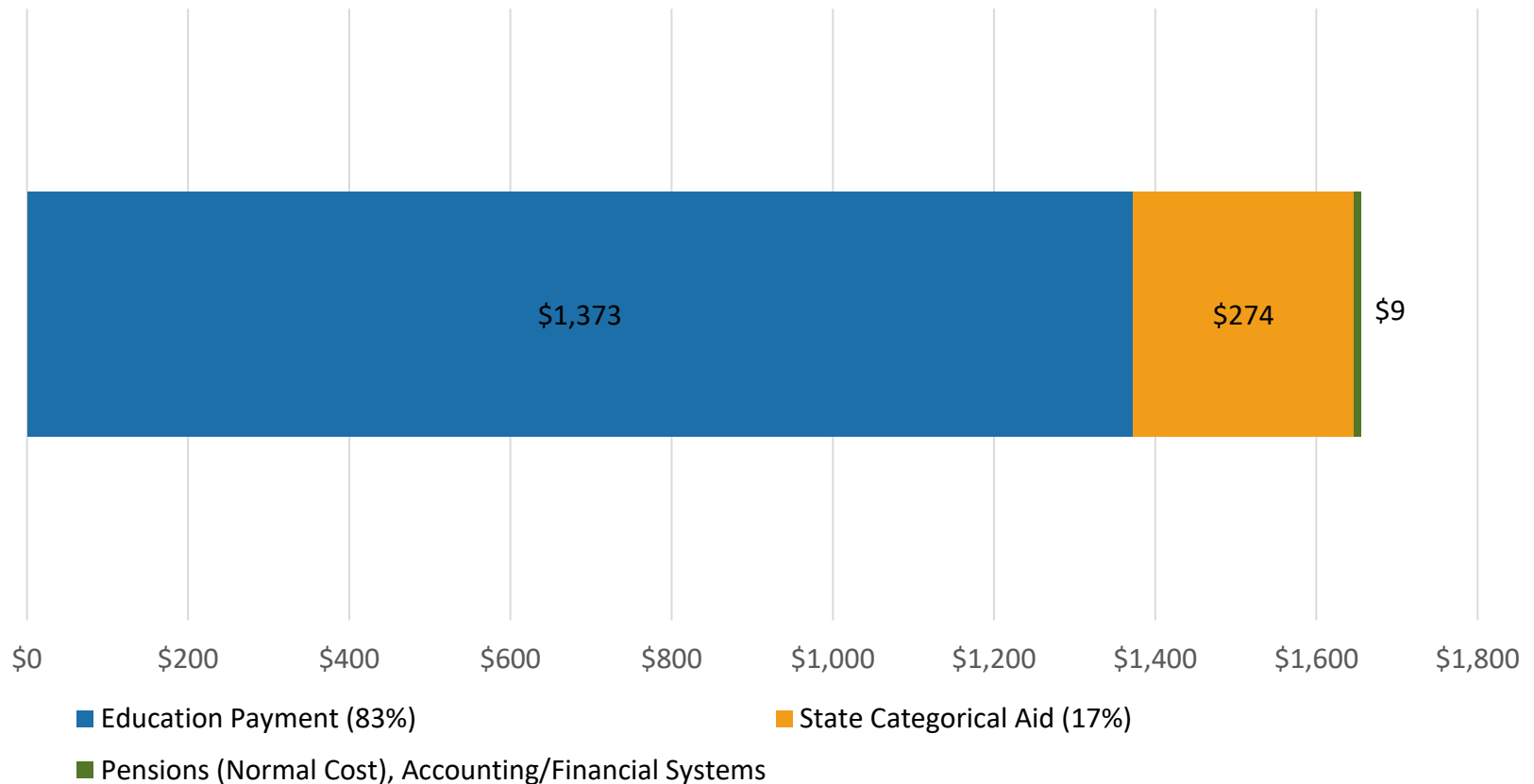


Beginning in FY2019, the statutory general fund transfer to the education fund was replaced with dedicated revenue from the 100% sales & use tax and a 25% of the meals & rooms tax.

EDUCATION FUND USES

Nearly all uses are direct payments to school districts in the form of state categorical aid or the education payment.

FY19 Education Fund Appropriations (\$M)



State categorical aid includes special education aid, technical education aid, transportation aid, state-placed students, small school support, and flexible pathways.

THREE TAX BASES SUBJECT TO THE STATEWIDE EDUCATION TAX:

Nonhomestead Property

- All taxable real property that does not qualify as a “homestead” – for example, commercial & industrial property, rental housing, second homes, etc.
- The nonhomestead property tax rate is uniform across towns.

Homestead

- A resident’s home and all contiguous land.
- The homestead property tax rate in each town varies directly in proportion to per-pupil education spending.
- A housesite is a subset of the homestead – the housesite includes no more than two acres of contiguous acres. The property tax credit is linked to the housesite.

Household Income

- Broadly defined to include all income, taxable and nontaxable, of everyone who resided in the household at any time during the tax year, including children and unrelated individuals.
- The tax rate on household income in each town varies directly in proportion to per-pupil education spending.

Yields/base tax rates are initially recommended so that all three types of property tax payers experience the same average increase in liability.

HOW ARE HOMESTEAD TAX RATES ADJUSTED TO ACCOUNT FOR PER-PUPIL SPENDING?

- By statute, the base homestead tax rates are \$1.00 for homestead property and 2% for household income.
- After voters approve their school budget, the base tax rates are adjusted by per-pupil education spending:
$$\text{\$1.00} \times (\text{per-pupil spending} / \text{property yield}) = \text{homestead property tax rate}$$
$$2\% \times (\text{per-pupil spending} / \text{income yield}) = \text{tax rate on household income}$$
- *Property and income yield, education spending and equalized pupil* are terms of art in Vermont education finance defined in the three following slides.

WHAT IS EDUCATION SPENDING?

- Voters approve **budgeted spending**.
- **Education spending** is budgeted spending minus the following offsets:
 - Federal aid
 - State categorical aid
 - Other expected revenues/offsets

WHAT IS AN EQUALIZED PUPIL?

- The objective of calculating equalized pupils is to create an “average” student in terms of assumed costs for a given district
- Specific categories of students are presumed to have different costs than other categories
- Cost categories that are differentiated are: grade of study (pre-k, secondary students), economically disadvantaged students and English language learners
- Equalized pupils are based on a two years of Average Daily Membership data (ADM) – this is the number of full- time equivalent resident students whose education is paid by the district from the 11-30th day of the school year (October) plus the number of state placed students

EXAMPLE – ANNUAL SCHOOL DISTRICT MEETING

Article X - Shall the voters of the school district adopt a budget of \$25,324,090 which is the amount the school board has determined to be necessary for the ensuing fiscal year? It is estimated that this proposed budget, if approved, will result in education spending of \$16,924.25 per equalized pupil. This projected spending per equalized pupil is 2.45% higher than spending for the current year.

Budget = \$25,324,090

Categorical Grants and Federal Offsets = \$4,083,649

Education Spending = \$21,240,441

Equalized pupils = 1,255.03

Education Spending per equalized pupil = \$16,924.25

WHAT IS THE “YIELD”?

- The yield can be thought of as the per-pupil amount of spending that can be supported with a uniform homestead tax rate of \$1.00 on homestead value or 2% of household income.
- In FY2019, the property yield was \$10,220 per pupil. The income yield was \$12,380 per pupil.
- The homestead property and income tax rate in any district spending more than the yield is increased proportionally.
- Whether a resident homeowner pays the education tax on homestead value or income, the tax rate increases in proportion to per-pupil spending.

- Back to our example, for the district spending \$16,924.25 per pupil:
 - The homestead property tax rate is:
Per-pupil spending / yield x \$1.00 = (\$16,924.25 / \$10,220) x \$1.00 = \$1.656
 - The income tax rate is:
Per-pupil spending / yield x 2% = (\$16,924.25 / \$12,380) x 2% = 2.73%

WHAT IS THE COMMON LEVEL OF APPRAISAL (CLA)?

- Since the education property tax is administered locally, it is necessary to adjust property values to account for differences in appraisal levels across towns.
- The CLA is a measure of how close each town's local appraisals are to the actual fair market value (FMV) in that town.
- The CLA is determined annually through the *Equalization Study* prepared by Property Valuation & Review.

Example:

- Town Y which sends all their students to district X has CLA of 89%
 - The grand list in Town Y is valued lower than the current fair market value (100%)
 - *The town may be considering reappraising*
- The tax rate experienced by tax payers in town Y is the calculated district rate adjusted by the CLA $\$1.656/89\% = \1.861

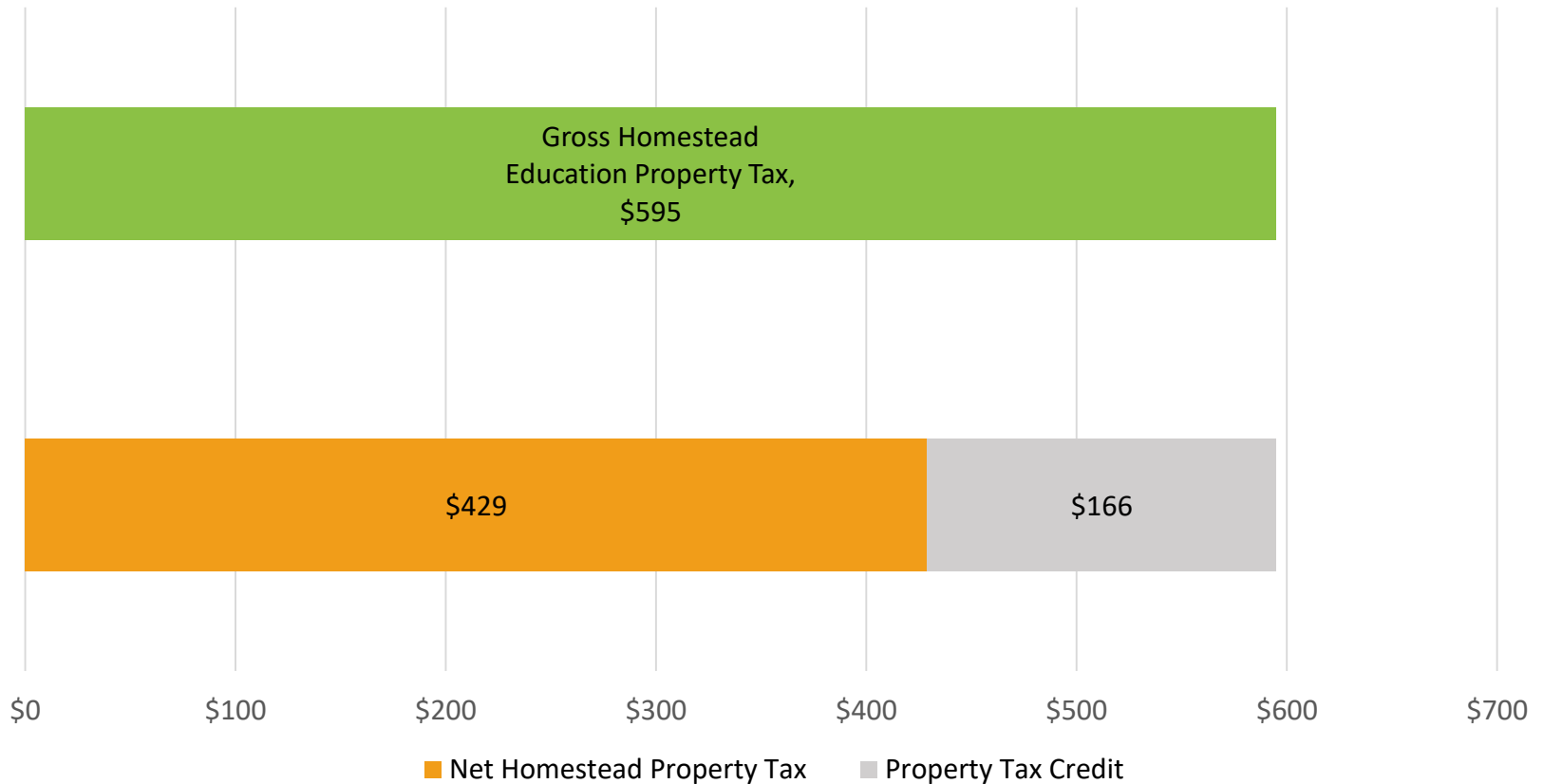
PROPERTY TAX CREDIT

- Property owning residents of Vermont are eligible for assistance/to pay property taxes based on their household income
- The property tax credit is limited to the housesite (home and two acres). The full homestead property tax rate is owed on additional contiguous acreage.
- The credit is calculated by comparing the housesite education property tax paid and the maximum amount the resident was eligible to based on a percentage of their household income in the calendar year.
- Property tax credits are applied to property tax bills in the following tax year.
- The income rate is adjusted each year based on local education spending in the same manor as the homestead education property tax (recall the income yield).

PROPERTY TAX CREDIT

About two-thirds of resident homeowners are eligible for an income-based adjustment to their housesite property tax.

FY19 Homestead Education Tax (\$M)



The property tax credit applies only to the “housesite”, a residence and up to two acres of contiguous land

HOMEOWNER REBATE

Resident homeowners with household income under \$47,000 are entitled to additional tax relief if their education and municipal town property taxes exceed a fixed percentage of income.

| Household Income | Maximum Education Liability | Maximum Municipal Liability |
|--------------------|-----------------------------|-----------------------------|
| 0-\$10,000 | 0.5% | 1.5% |
| \$10,000 -\$25,000 | 1.5% | 3.0% |
| \$25,000-\$47,000 | 2.0% | 3.0% |

SUMMARY – TAKE A DEEP BREATH!

1. Vermont has a unique education finance system - a statewide funding formula coupled with local administration.
2. School boards set budgets and submit them to voters for their approval, maintaining local control over education spending.
3. The Legislature sets the yields and base education property tax rates annually at the level necessary to fund voter-approved school budgets.
4. Our education system may be viewed as either an income tax system or as a property tax system with adjustments for income.
5. Whether assessed on property value or income, homestead tax rates vary with local per-pupil spending.
6. The nonhomestead tax rate is uniform statewide, not directly related to local per-pupil spending.

ADDITIONAL RESOURCES

Legislative Joint Fiscal Office – Education Finance <https://ljfo.vermont.gov/subjects/education>

Agency of Education – Data & Reporting <https://education.vermont.gov/data-and-reporting>

Department of Taxes – Property Owners <https://tax.vermont.gov/property-owners>