

**Task Force on the Implementation of the Pupil Weighting Factors Report
Testimony of Stephanie Yu, Deputy Director, Public Assets Institute
November 19, 2021**

1. **Introduction.** My name is Stephanie Yu and I'm the Deputy Director of Public Assets Institute. With me is Jack Hoffman, our Senior Policy Analyst. When I was here last a couple of months ago, I gave a quick overview of the education funding system, and there are two points I'd like to remind you of before digging into income-based taxes for residents and what that would mean.

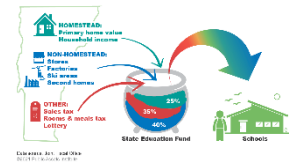
a. First, unlike almost every other state, Vermont has a statewide school tax



system. We all collectively pay for all the kids. So in Vermont, how much your community can raise does not determine how much you have to spend on education. Instead, we calibrate districts' tax rates so they correspond to per-pupil spending. Vermont's system supports whatever spending level voters choose, but towns with more spending per pupil have higher tax rates;

those with lower spending per pupil have lower rates, and towns with the same per-pupil spending have the same rates. We all contribute to the statewide Ed Fund proportionally based on the per-pupil spending we vote in our town.

All school taxes go into a single pot—the state Education Fund Resources available to a school are not based on the dollars generated by the community.

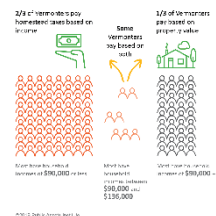


b. Second, resident taxpayers can pay their school taxes in one of

two ways: either based on their primary home's property value or on their household income. And what we collect from these is what we call homestead taxes – about 25% of the total Ed Fund. We have the income option because we recognize that paying strictly based on property value is regressive – meaning lower-income Vermonters pay a greater share than those with higher incomes, and for those with fixed incomes, rising property values make it tough for them to stay in their home. So for most Vermonters, paying by income is the better deal and makes the system less regressive. But for those at the high-end of the income scale, paying based on property value is the cheaper option.

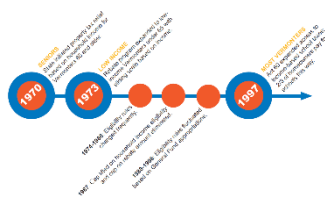
Two parallel systems

The way it has been



2. **An income-based system.** So we essentially have two parallel systems for how Vermont

Vermont has been moving toward income-based school taxes for 50 years



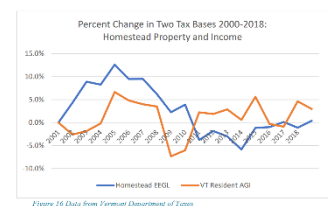
residents pay their school taxes: one based on household income and one based on property. The history of the transition to income-based taxes is a long one. In fact, back in the 1990s, when the Legislature was redesigning the education funding system, the House passed an income-based system that was rejected by the Senate. But even

property system or income system was the best option. One of the most important findings of the Commission was that home value is not a good measure of ability to pay. At the low end, property values may exceed a family's net worth because they owe a lot on their mortgage and have few other assets. And at the high end, your primary residence is a small slice of your total net worth. In neither case is it a good indicator of what you can pay. Ultimately, you pay your taxes out of your income, not your property.

3. Here's how it would work:
 - a. All Vermont residents pay school taxes based on income.
 - b. Tax rates, as they are now, will continue to be determined by per-pupil spending approved by local voters on TMD.
 - c. All housesites are exempt from school property taxes.
 - d. A housesite is a primary residence and up to 2 acres of adjacent land.
 - e. All property other than housesites will be taxed at the uniform nonresidential rate set by the Legislature each year.
 - f. Renters pay school income rate, but receive credit for landlord's school property taxes paid through rent.

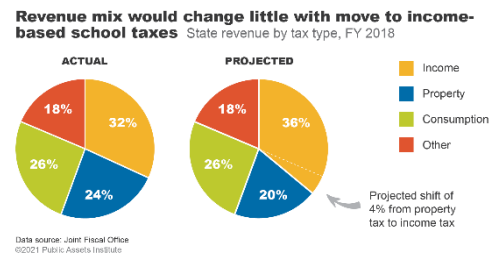
So everyone would pay through the same system based on the best measure of their ability to pay – their income. The system would move the remaining 1/3 of Vermont homeowners – the high-income ones- to paying based on income, which would be much fairer. And it would be a lot simpler. Calculating your taxes on Town Meeting Day would only require knowing your income and the tax rate, unlike the 24 steps you need to go through now according to the Tax Department.

4. So what's stopping us? If a nonpartisan Commission said income-based school taxes are the way to go, and we've been pushing for them for 25 years, what's the problem?
 - a. One of the most consistent arguments we've heard against income-based taxes over the years is that income is more volatile than property so it's a less reliable revenue source. But the Tax Commission did a great job of addressing this as well, and what they found was that the income tax base was actually less volatile than the property tax base from 2000-2018. As you can see in this chart, both tax bases are moving around quite a bit. We'd also add that the issue of volatility is really about who absorbs any volatility – the state or the taxpayer. From the state's perspective, property revenue might look more stable, but that's only because we adjust the rates each year to raise what we need. So even when property values change, the state still gets the revenue it needs. But from the taxpayer's perspective, you want your tax bill to go down when your income goes down.



Again, people pay taxes out of their income, not their property value, so it makes sense that their tax bill moves with their income, not their property value.

- b. The second argument is about relying too much on income-based taxes. This is really two concerns that get conflated: first, concern about the overall reliance in the state's whole revenue system on income-based taxes, and second, concern about Vermont being perceived as a high income tax state. To answer the first part, this change would only have a modest effect on the mix of taxes overall – we'd go from 32% of all state revenue being income-based taxes to 36%. Not a huge shift. Total state revenues are around \$4B and we're talking about moving \$150-200M from a property tax to an income-based tax. This isn't touching the nonhomestead property taxes at all, which are 40% of the Ed Fund. And on the second concern, Vermont has a progressive income tax system, meaning that the state is not a high tax state for low- and middle-income people. And the research is very clear, including our own analysis of Vermont migration as well as national work on this, that state income taxes do not drive people to move out of state.



5. A lot of good work has gone into showing the benefits of an income-based system, and alleviating any concerns about it, which is why we're glad this conversation is moving forward. We appreciate your work on this, and your recognition that a fair system of who pays what is very much tied to how much communities can invest in their schools overall.

Conclusion. Vermont has a solid education funding system with a baseline level of statewide equity for students and taxpayers balanced with local control over school budgets. It is a complicated system that can and should be made much simpler. It is much more equitable than those of other states and we should be building on that equity. There is a lot of overlap in how the two issues you're considering – pupil weighting and moving to income-based taxes—impact students and voters. I think a useful way to think about them is that income-based taxes would improve the system's basic level of equity where all students have access to the whole pot of resources and school districts make the same tax effort for the same per-pupil spending. Income-based taxes correct a current unfairness – that higher-income Vermonters pay a smaller share of income in school taxes than low- and middle-income ones. The other conversation you're having is about that second level of equity—making sure all kids have the resources they need, whether through pupil weighting, categorical aid or some other tool. And that second level does need to be brought up to date now, and periodically tweaked to keep up with the changing needs of students. Both are important improvements to the system, and we hope we can make progress on both this year.



We all have a stake in every child's future

Before Act 60 'our kids' meant the kids in our own town



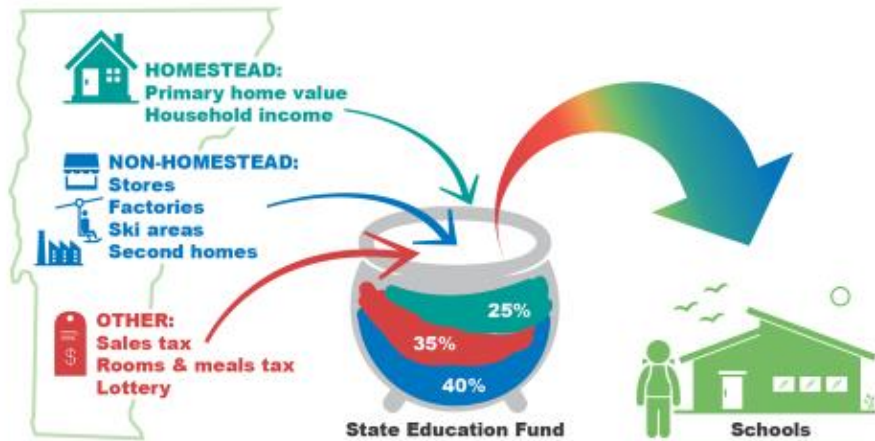
Since Act 60 'our kids' includes all the children in Vermont



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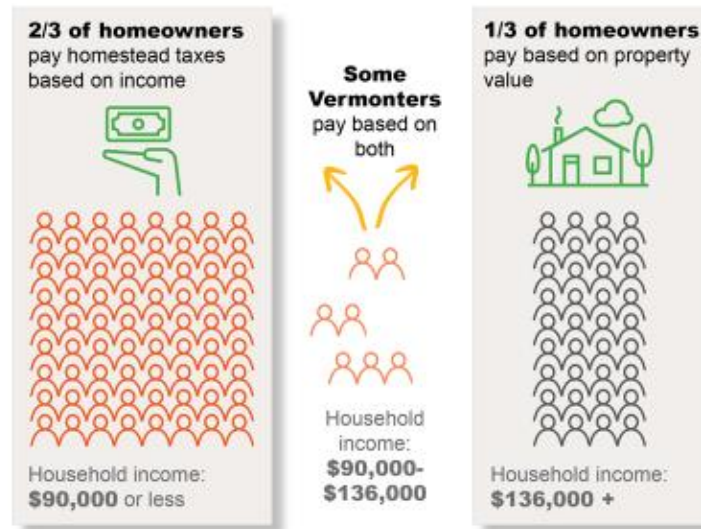
All school taxes go into a single pot—the state Education Fund Resources available to a school are not based on the dollars generated by the community





Vermont school funding: two parallel systems

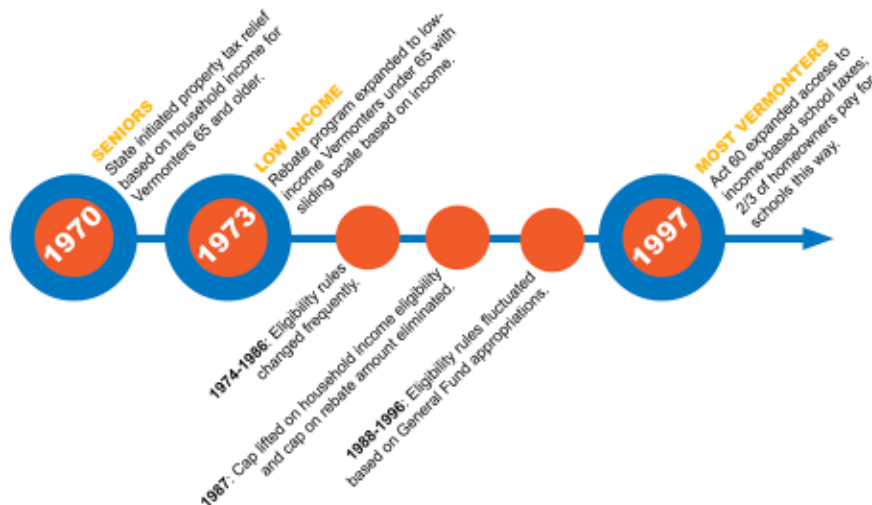
The way it is now



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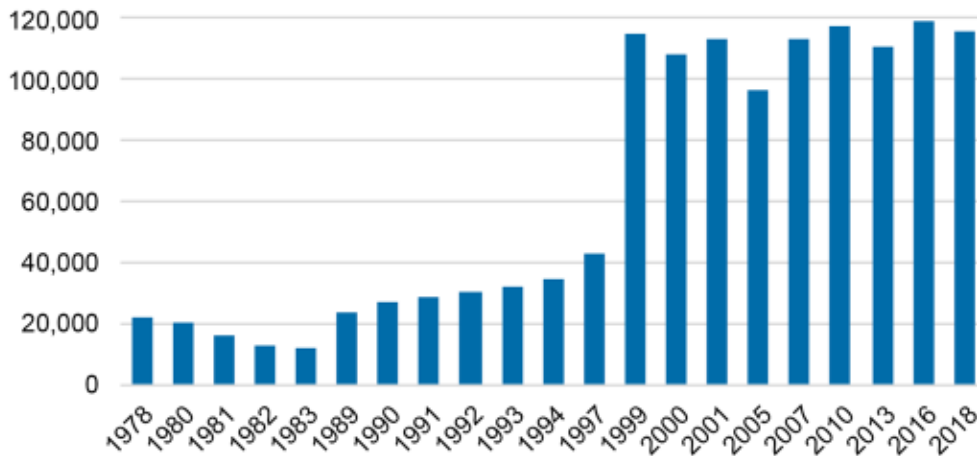
Vermont has been moving toward income-based school taxes for 50 years



Data source: Joint Fiscal Office
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More and more Vermonters take advantage of income-based school taxes Households paying by income, selected years 1978-2018

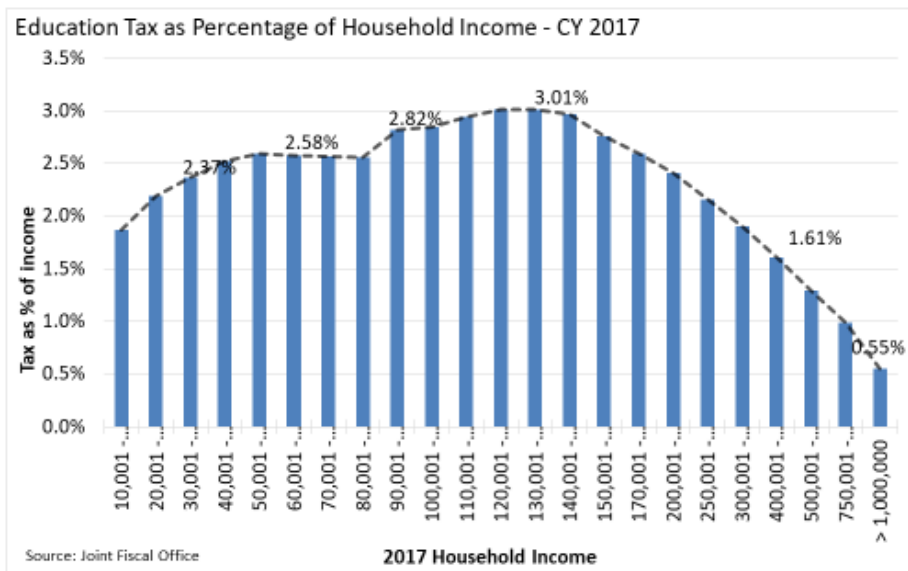


Data source: Vermont Department of Taxes
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The system is skewed toward high-income Vermonters

Those who pay based on property tend to pay a smaller share of income





The Tax Structure Commission found that both the property and income tax bases change over time

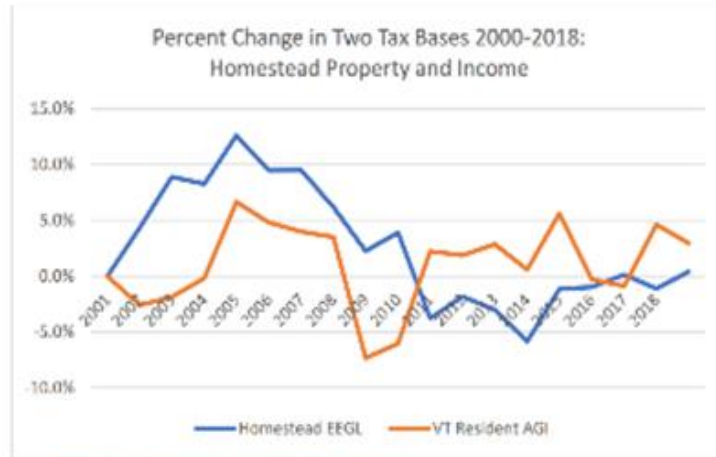
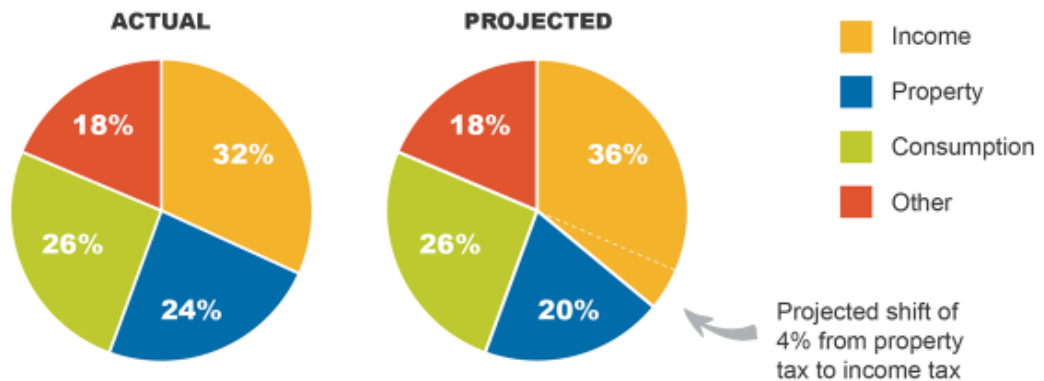


Figure 16 Data from Vermont Department of Taxes

From the Tax Structure Commission final report February 2021

Revenue mix would change little with move to income-based school taxes State revenue by tax type, FY 2018



Data source: Joint Fiscal Office
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