

September 11, 2020

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Vermont Tax Structure Commission

Re: Follow up to August 31 testimony

Dear Commissioners:

Thank you for inviting me and our deputy director Stephanie Yu to your meeting last week. We appreciated the opportunity to review with you some of the key reasons we believe that eliminating the school property tax on primary residences is good public policy and how making this change would create a fairer, simpler school funding system for voters and taxpayers.

I want to review and expand on some points that were addressed at the August 31 meeting:

1. Direct-democracy decision-making: Public education is locally controlled in Vermont, and that is a strength of the system. School district residents are closest to the children in their schools. They vote each year on the amount they want to spend on their children's education, and their voted spending directly impacts the district school tax rate that they pay. Higher per-pupil spending results in higher tax rates in the district. It's the same for all the districts in the state. Based on the yield set by the Legislature each year, any two districts with the same per-pupil spending have the same tax rates. This is true for both income and property rates set for each district.

This direct-democracy process with tax consequences directly tied to voters' decisions is the most publicly accountable system we have in Vermont. It allows district residents both to elect school directors who propose the budgets and to vote on approval of those budgets, balancing school spending levels with their tax bills.

2. Property vs. income: More Vermonters could participate in school budget votes if the state made the system simpler for them. Many voters find the school funding system too complicated to readily understand the tax impact of the school budgets they're asked to vote on, as we noted during our testimony. This has led to confusion, misunderstanding, and complaints. A voter needs at least seven pieces of information and must do several math operations to estimate the school tax on a home. The school tax on primary residences moves up or down depending on the school district's per-pupil spending.

The main reason for this complexity is that the system is trying to merge two different taxes, property and income. Income has been acknowledged as the best measure of ability to pay since 1969, when Vermont instituted a property tax rebate program for senior citizens. And the property tax has been shown repeatedly to be regressive and unfair. So Vermont has been adjusting the school

property tax on primary residences based on income, as a way to bring ability to pay into the tax calculation. The result is a complicated system that no one can understand or explain. To make the system understandable for voters, the state needs to choose one of the two options for a statewide tax paid by residents with rates that can be set in each school district based on spending per pupil. Property and income are the two options. We recommend an income-based tax as the fairest, simplest one.

3. Circuit breaker: By eliminating the current school property tax for homeowners, the state would leave in place the income-based tax with rates set for each school district based on its per-pupil spending. The current minimum income-based tax rate for any school district is 2 percent of household income. While we recommend shifting to adjusted gross income (AGI) in place of the current more complicated household income, we don't expect this minimum rate to change much.

Households with incomes of less than \$47,000 are currently eligible for a credit to ensure that they pay no more than 0.5 percent, for the lowest income families, to 2.0 percent of income for those nearer \$47,000 [32 V.S.A. § 6066 (a) (4)]. Since households eligible for this circuit breaker currently pay a lower percentage of income than the minimum school district income rate for homesteads, shifting to an income-based tax likely will require a circuit breaker.

Using AGI, however, will simplify administration of the circuit breaker by allowing individuals with incomes below the eligibility threshold to pay a percentage of the income-based tax on a simple sliding scale included on the income tax form. Using this method, those eligible for the circuit breaker reduction would see their school taxes go up or down with their school district's spending per pupil, directly connecting their taxes with their district's spending decision.

4. Education Fund Advisory Committee: Some of the issues that have created confusion and frustration with the school funding system are the result of the lack of coordinated system management. School finance has many moving parts that affect the taxes that Vermonters pay in each school district. Property values move up and down, which affects tax rates. The Legislature has made many changes to the system that have further confused Vermonters trying to make sense of it. Political decisions to stabilize property taxes by using Education Fund reserves one year have resulted in sharp property tax increases the next year. The school funding system would benefit from a stabilizing management structure. We recommend that an Education Fund Advisory Committee be established.

Vermont has a good model in the Capital Debt Affordability Advisory Committee created by the Legislature in 1989. The Committee reviews the affordability of the state's debt each year and recommends a maximum amount of new long-term general obligation debt for the next fiscal year. The committee's recommendation is advisory, but because it has been accepted as the state's bonding limit by elected officials, it has brought order and rationality to what had been a chaotic process for years.

An Education Fund Advisory Committee would provide similar stability for the school funding system. A committee that regularly monitors the various factors that affect school taxes would make recommendations to the Legislature each year for the residential tax yield, non-homestead tax rate, and use of reserves as well as recommendations for any needed system adjustments.

We understand that school funding systems are complicated in part because they involve coordination between the state and localities. But Vermont's system can be made much simpler for voters, who are also taxpayers. These are the key people who make the school funding system work so that Vermont can provide an excellent education for our students.

We appreciate the effort the Commission is making to understand the issues with the system and to explore options for improvements. We remain convinced that eliminating the school property tax on Vermont's primary residences would be a big step forward. And we would be happy to meet again with the Commission to think with you about the system changes needed to make that happen.

Sincerely,

A handwritten signature in cursive script that reads "Paul A. Cillo". The signature is written in black ink on a light-colored background.

Paul A. Cillo
President