

# Memorandum

To: Vermont Tax Structure Commission  
From: Paul A. Cillo, Public Assets Institute  
Date: December 17, 2020  
Re: Comments on the Commission's draft report

---

We recognize that you are still revising various parts of your report, and we can imagine that you all are eager to wind up this two-year effort. We will keep our final comments brief.

- 1. Consumption taxes.** The drafts to date make a good case for reducing or eliminating the exemptions for consumption taxes. They also have been clear about the need to protect low-income Vermonters who will find it burdensome to pay these inherently regressive taxes. It appears the Commission plans to leave it to the Legislature and the Tax Department to develop a mechanism to credit, rebate, or otherwise offset the consumption taxes paid by low-income residents. That makes sense. But we would encourage the Commission to include recommendations for how the mechanism should work. For example, rebates or credits can be a problem because the relief comes once a year and after the fact. However low-income taxpayers are made whole, it would be best if they don't have to wait for a refund. Ideally, the mechanism to rebate or refund consumption taxes should be a tax expenditure rather than an appropriation. Unlike tax expenditures, appropriations can be separated from their purpose, which makes them vulnerable to cuts in times of budget stress.
- 2. Income-based education taxes.** In your drafts and exchanges about an income-based education tax, we appreciate your emphasis on simplicity and fairness. We certainly believe those are two important features of an income-based tax. But both bear repeating, especially the fairness aspect. We still see and hear messages that seem designed to stigmatize the income-based education tax. The property tax is portrayed as the correct way to fund education, and those who don't pay the property tax are somehow not paying their fair share. For example, the Tax Department's Property Tax Credit reports include this definition of the Total Education Credit: "The total amount of education property tax credit granted. This represents lost FY20 revenue for the education fund." In other words, the Education Fund is being short-changed because some people are paying an income-based tax. Vermonters who pay school taxes based on the homestead income rate are paying what the Legislature has determined is their fair share. By moving to an income-based tax for all residents, perhaps we can finally agree that everyone is paying their fair share.
- 3. Progressivity.** As we read your various drafts, we also reviewed our own testimony and the testimony from others. When we testified in late August about the regressivity of Vermont's overall tax structure, we overlooked the report submitted by the Vermont Futures Project. We both drew on a study by the Institute on Taxation and Economy Policy (ITEP), the sixth edition of "Who Pays?", but clearly read it differently. On page 4 of its report, the Vermont Futures Project says the ITEP study "indicates that the Vermont tax structure is already highly progressive." The accompanying ITEP chart shows Vermont with an "inequality index" of +1.5 percent.

According to the ITEP methodology, however, the positive index does not signify that Vermont's tax system is highly progressive. As ITEP explains: "In states with positive tax inequality indexes, incomes are at least somewhat more equal after state and local taxes than before." The full index, which is included in Appendix B of the study, shows that low- and middle-income Vermont taxpayers still paid a slightly larger share of their income in taxes than did those in the top 1 percent income bracket. The ITEP study found Vermont's tax system, while better than most, was regressive.

We work frequently with ITEP, and we contacted Aidan Davis, senior analyst, to ask her to clarify ITEP's inequality index. Her email response is attached.

## Jack Hoffman

---

**From:** Aidan Davis <aidan@itep.org>  
**Sent:** December 17, 2020 6:10 PM  
**To:** jack@publicassets.org  
**Subject:** ITEP Response

Jack,

It was great to hear from you.

Here are my thoughts/comments. Please let me know if there's anything you'd like to discuss.

ITEP's Tax Inequality Index is a measure of the impact each state's tax system on income inequality. It examines whether the gap in families' shares of income is wider or narrower after state and local taxes. In the sixth edition of *Who Pays?*, we identify states with more equitable state and local tax systems. Six states, Vermont included, report positive scores on the Index, meaning that their state and local tax systems do not worsen income inequality. But that's not to say that these tax systems are robustly progressive, where the lowest-income taxpayers pay the smallest amount as a share of income and taxes increase with each income level.

Our analysis of Vermont's state and local tax system identifies that there is still room for improvement on the measure of tax equity. For instance, Vermonters in the middle quintile—with incomes between \$39,000 and \$60,000—pay more as a share of their income in state and local taxes than those with incomes between \$60,000 and \$94,000. Similarly, those with incomes between \$94,000 and \$196,000 pay more as a share of their income than those with incomes between \$196,000 to \$460,000.

Perhaps most notably, our analysis concludes that the top 1 percent of earners, with incomes in excess of \$460,000, currently pay an overall state and local tax rate that is very similar to the rate paid by large numbers of families closer to the middle of the income distribution. That is, the rate paid by this affluent group is within 0.3 or 0.4 percentage points of the rate paid by families earning between \$39,000 and \$60,000, as well as families earning between \$94,000 and \$460,000. This lack of meaningful progressivity in taxing top earners is a notable departure from Vermont's strong progressive tradition in other policy areas. By definition, Vermont's top earners are much more able to pay a higher tax bill than the vast majority of families. And yet together, the state and local governments ask these fortunate individuals and families to pay a rate that is nearly identical to the rate it charges the state's middle-class.

My source: <https://itep.sfo2.digitaloceanspaces.com/Vermont-total-graph.jpg>

My best,

Aidan Davis  
Senior Analyst  
Institute on Taxation and Economic Policy  
202.299.1066 x30