

**Memo To: Vermont Tax Structure Commission dated 1/20/21**  
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**In this memo I will provide some comments concerning the recently released draft of the TSC report. I will confine my remarks to the Education Finance Chapter 6 since that is the topic that I provided input earlier to the Commission. In this first section I summarize the concerns that I have, and then I go through several topic with more detail.**

## **SUMMARY.**

**The TSC recommends replacing the Homestead education property tax on a house site and two acres with a variable and voter determined income tax on Adjusted Gross Income. All homestead property surrounding a declared house site beyond the 2 acres would be taxed at the uniform Non Homestead property tax rate. The education income tax would be adjusted based on locally voted education district spending in the spring of any given year, and applied to the AGI of the previous year. Further, the TSC recommends establishing an Education Tax Advisory Commission to evaluate matters connected to education finance and to make recommendations to the Legislature and the Administration on a regular basis.**

**While I am open to this approach, the report does not have enough information for me to evaluate the implications of this shift. I may be expecting too much from the Commission given the scope of their assigned mission, but the absence of illustrative numerical examples and charts that would allow a reader to compare the implications of the recommended approach to that of the current framework undermines the validity of those recommendations.**

**I think it may be useful to separate the house site and 2 acres from any larger surrounding acreage and to impose the education income tax to all those who declare that homestead. But I don't understand the implications of shifting Homestead property beyond the 2 acres around the house site to the Non Homestead category for a fixed statewide tax.**

**I also don't understand the implications of going from the Household Income to the Adjusted Gross Income in terms of what is taxable as the best representation of "ability to pay" and in terms of whether the change alters what I see as the current disincentive for shared housing.**

**The TSC asserts that any problems of timing related to school budgets and the variable education income tax rates for voters can be resolved. I would like to hear confirmation of that from those who would be involved.**

**I am deeply disappointed that although the TSC mentions the issue of which costs should be covered by the Education Fund and which should not, it passes this topic on to some possible future advisory commission rather than applying the words of the statute literally. It seems to me that this issue should be central to education finance – not just which taxes to use, but also what is to be financed.**

**I continue to believe that an approach that imposed a fixed progressive education income tax surcharge within our existing income tax system, that retained a variable and voter determined homestead property tax at a lower level, and that removed from the Education Fund any and all costs not directly related to education and directly voted on by local district voters might be superior to that proposed by the TSC.**

## **EXTENDED COMMENTS & QUESTIONS.**

The TSC has recommended switching to an education income tax on all Vermonters who own a house and up to 2 acres around it. All other property immediately surrounding a house site beyond the 2 acres would be re-classified as Non Homestead property and taxes at that statewide rate. The income tax base would be Adjusted Gross Income.

**ISSUE #1:** The TSC provides no illustrative examples of this recommendations either at a macro or a micro level to show how it might work in practice and how the tax burdens of education financing would shift. This is a grave omission. Such examples are essential to any evaluation of whether the proposal meets the professed goals.

**Q1:** Why does the TSC not use the Education Fund Outlook framework to show what the various rates might be in different scenarios? A past year could be used for which all data is available.

**Q2:** What might be a possible average education income tax rate be to raise the same amount of tax revenue as that raised by the net homestead tax in the chosen illustrative year? Alternatively, what would be an appropriate rate and how much would it raise? Examples illustrating 2%, 2.5% rates would be useful, bearing in mind that this would be an average since the set base rate would vary with spending levels approved by local voters.

**Q3:** Given a certain average education income tax rate, what might the Non Homestead property tax rate be, when the additional grand list value from the formerly Homestead property is incorporated? What balance or relationship would there be between the amount of revenue to be raised from the Education Income Tax and that raised from the Non Homestead property tax?

**Q4:** What is the amount of the value of the Grand List property that is being switched to the Non Homestead property category – the property beyond the house site and 2 acres? I know that likely the bulk of house sites is encompassed by the house and 2 acres measure, but outside of our most densely settled areas there may be significant property that is being switched from the now defunct Homestead property tax category and into the Non Homestead Property tax category. For instance, if a house is on a 10 acre lot, and all of it is developable, the 8 acres re-classified from HS to NHS might amount to a significant value, and therefore potential change in tax liability. How much is this and how is it distributed across the income distribution? This might be a smaller issue than I think at the aggregate level, but it still could mean significant changes in particular cases. And the shift of this property to the statewide tax reduces cost control as the tax is no longer voted by local districts.

**Q5:** What are the equity or distributional issues involved in changing the taxation of that previously Homestead property to the Non Homestead category? In general, the Non Homestead property tax rate has been higher than the AVERAGE Homestead property tax rate. In the kind of illustration that should be done of this recommendation, does the NHS property tax rate come down, or go up, or stay the same? If there is an example in which the same amount of revenue is raised on the new HS income tax as the net amount from the net HS property tax under the current framework, aren't there equity issues if the formerly Homestead property will now be taxed at a higher rate than before for residents of many towns? I believe that there may be Towns for which under the current system the NHS rate is actually lower than the HS rate. Does it make sense that those property owners get a tax cut?

**Q6:** Why didn't the TSC provide expanded versions of Figures 13 and 14 to show the distribution of ownership of Homestead property beyond the house & 2 acres and in Figure 15 differently colored bars

showing the total homestead taxes paid when the current taxes on these properties are incorporated? This might make it possible to see whether this is a significant issue or not.

**Q7: Why didn't the TSC provide examples of how education tax liabilities would change under the recommended regime compared to the current regime for individual taxpayers in particular situations?**

**ISSUE #2: There are no numerical illustrations of the implications of the shift from Household Income to Adjusted Gross Income as the tax base representing the "ability to pay".**

Under the current system a Homestead Declaration is accompanied by a Household Income form that aggregates the income for all members of a household as the basis for setting the tax due. I am not clear about the implications or details of the switch to using Adjusted Gross Income.

The Household Income form has been the source of considerable complexity and confusion for Vermonters in completing their tax returns, so on the face of it going to Adjusted Gross Income makes a lot of sense. However, AGI excludes certain kinds of income and transfer payments that are included in HHI. Are the implications of that change desirable and intentional? Whose measure of "ability to pay" goes down, and does the change make sense?

I have long been concerned about the way in which it appears to me that the HHI approach to the determination of education taxes owed has penalized Vermont homeowners who live together. It would seem to me that one way to make the most of our housing stock, to use our housing stock efficiently, would be to encourage people to live together where feasible, or at the very least not to penalize them for doing so. Under the current system, if a parent with an income that makes them eligible for the property tax credit lives alone, their education taxes will be at a certain level based on their income. If their adult son lives with them, who may or may not be able to help with expenses, their household income is likely higher, and their education tax liability will be higher.

**Q1: So under the proposed system, would a person still declare the homestead and list the members of the household, who are then taxed on their individual AGIs separately through billing by the tax department?**

**Q2: How do the tax liabilities under the new system with AGI compare to those under the current system of property tax credits for those that are eligible using HHI? The TSC should provide illustrative examples. There might be particular differences that might be arbitrary or might be desirable.**

**Q3: As in the current system, is there still a substantial incentive for Vermonters NOT to share their home with others? Or even to leave out of their list people who are actually in their household?**

**Q4: Why didn't the TSC show Figures 13, 14, and 15 with household AGIs instead of HHI, or is that impossible from a data perspective? It would be interesting to see how the numbers would be different both under the existing regime and under the proposed regime.**

**ISSUE#3: What costs are in the Education Fund and the "ETAC".**

I am deeply disappointed in the failure of the Commission to fully address the issue of which costs should be financed by the Education Fund.

In my comments earlier in the year I noted that the cost of the Property Tax Credit and the cost of Current Use to the Education Fund could be seen as illegitimate under the statutory language that

established the Education Fund, since neither have been approved by local voters and they do not directly concern education, and before there was an Education Fund these costs were paid for in the General Fund.

The Current Use program costs some \$46 million in lost property tax revenue in order that agriculture and forestry landowners can based on the income from their property rather than the property value. This is an important program but it is not education, it is not approved by local voters, and the cost is not even consistently listed in the Education Fund Outlook.

Very least, recommend that cost be included in Education Fund Outlook. As of now need to go to the property value report and know what to look for.

The recommendation of shifting to an education income tax eliminates the apparent annual cost of the PTC, although there will still be an internal shift in costs with that change even though it would be disguised. The TSC has not provided an estimate of that shift in tax burden.

At the very least the TSC might have recommended that the Education Fund Outlook should in some manner consistently list the costs of Current Use, of the Tax Increment Financing, of the Act 46 incentives while they last, and of any other hidden costs so that legislators and voters know what is being financed.

The concept of the Education Tax Advisory Committee is a good one, and perhaps this issue of what is in and what is out could be contemplated further by such a body. But again, the failure of the TSC to draw the obvious conclusions from the statutory language of Act 60 strikes me as both an intellectual failure and a failure of nerve.

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