FEASIBILITY STUDY*:*
Electronic Administration, Billing, and Collection of the Education Property Tax

Vermont Department of Taxes
July 15, 2011

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EXECUTIVE SUMMARY

The Legislature required the Tax Department to examine the feasibility of State administration of the billing and collection of the education property tax. The feasibility study asks three basic questions after reviewing the background of the education finance system:

1. What is the current distribution of billing and collection functions between the State and local jurisdictions?
2. What policy changes and resources are required to implement a proposed system in which the State bills and collects education property tax?
3. What are the potential impacts of this change on the Department of Taxes and its key stakeholders?

The answers to these questions provide Vermont's policymakers with information to better understand the decisions, resources, and timeline that will accompany a policy choice to have the State bill and collect the education property tax.

Current System

The study reviews the assessment, tax, payment, and delinquency functions executed by local and State government to administer the education property tax. Appraisal, billing, collection, and delinquencies are handled by local jurisdictions. The State has an advisory role with respect to listing practices and provides towns with the data necessary to bill the tax.

Also, the study describes the current state of administering property tax adjustments and the Tax Department's technology priorities. Property tax adjustments are discussed given their status as a key contributor to the Department's education property tax workflow. Specifically, approximately ten percent of Tax Department staff services property tax adjustments. Technology priorities are described given the impact a new technology priority, such as billing and collection of the education property tax, would have on existing priorities and how existing technology priorities may affect implementation of State billing and collection of the education property tax.

Proposed System

The study sets forth the policy changes, resources, and timeline necessary to allow the State to bill and collect the education property tax. Key changes include moving the local assessment calendar forward by three months, implementation of a new software system or a new module in an existing computer system, expansion of Tax Department personnel by approximately twenty percent, start up and ongoing tax processing costs, and a change to how the State accounts for and distributes tax revenue to school districts. Also, the study reviews myriad delinquency issues that would arise from state billing and collection, including the prioritization of liens, creation of a new abatement authority, tax offsets, and making the Education Fund whole in the case of late payment or non-payment by property owners.

Overall, the Tax Department estimates that technology implementation will take three years and cost between $1.25 million and $3.25 million. Ongoing personnel and processing costs once the system goes live are estimated to be at least $2.5 million annually to start. Currently, the State allows local jurisdictions to retain approximately $2 million to administer this tax, a revenue source that could defray the cost of State billing and collection in out years. Enactment in 2012 by the Legislature would allow the Tax Department to bill the education property tax by July 2015.

Potential Impacts on Stakeholders

The study describes potential impacts on various stakeholders, including taxpayers, local jurisdictions, real estate stakeholders, the Tax Department and the State.

- **Property owners** may experience increased clarity regarding the nature of the tax and education spending. Also, the bill may be more confidential. Yet, numerous redundancies will be created in billing, collection, customer service, and abatement functions among others as many services would be duplicated at the local and State level.

- **Local jurisdictions** would lose revenue from an inability to earn interest on education tax payments, removal of the State fee retained to administer the tax, and statutorily prescribed delinquent tax penalties.
- **Real estate stakeholders** would face significant unknowns as State billing and collection would change due diligence, tax payment, and escrow functions.
- **The Department of Taxes** would face significant opportunity costs in terms of its technology priorities. Also, State billing and collection would expand departmental personnel, materials, and budget.
- **The State** would be expanding during a time when many government institutions are contracting due to scarce resources.

Overall, it is not clear that State billing and collection would create significant efficiencies for stakeholders. Any duplication of services or addition of services will ultimately be reflected in the costs of the system and passed on to taxpayers.

CLA

Per legislative directive, the study examines variants of the Common Level of Appraisal (CLA) that are not applied to the tax rates. Specifically, the feasibility study reviews four variants of the CLA either applied independently to the product of the Equalized Tax Rate (ETR) and Listed Value (LV) or that adjust listed value by municipality.

INTRODUCTION

In 1997, Vermont's Supreme Court ruled the State's education funding system unconstitutional. In response, the legislature created a statewide education property tax. While a state tax, its administration is built upon the existing municipal property tax structure.[1] The reliance upon the local tax structure is perhaps most visible in the fact that Vermont's local jurisdictions bill and collect the state tax. The study fulfills the legislative requirement to examine the feasibility of the State administration of the billing and collection of the tax, ending the current piggyback upon municipal property tax billing and collection.

The feasibility study asks three basic questions after reviewing the background of the education finance system:

1. What is the current distribution of billing and collection functions between the State and local jurisdictions?
2. What policy changes and resources are required to implement a proposed system in which the State bills and collects education property tax?
3. What are the potential impacts of this change on the Department of Taxes and its key stakeholders?

The Department of Taxes aims to provide Vermont's policymakers and the Department's stakeholders with a greater understanding of the issues raised by State billing and collection of the education property tax. The report does not make recommendations, leaving this role to the Governor and Legislature.

1 Act 60 of 1997, the Act that created the education property tax, as passed originally by the legislature assigned responsibility for billing and collection of the education property tax to the Vermont Department of Taxes. Myriad issues arose, including the lack of a uniform parcel number system and a lack of technology resources at the local level of government. Accordingly, before State billing and collection went into effect the responsibility was shifted to local jurisdictions 1997 (Adj. Sess.), No. 71.

1.0 BACKGROUND INFORMATION

1.1 Statutory Mandate for Study

Section 45 of Act 160 of the 2010 legislative session requires the Department of Taxes to submit a feasibility report on "developing an electronic system for department's administration, billing, and collection of the education property tax provided for in Chapter 135 of Title 32" to the Joint Fiscal Committee. The legislature amended this mandate through Section 6 of Act 45 of 2011 by requiring the department to evaluate the feasibility of "application of the common level of appraisal separately and independently from the tax rate." This feasibility report is submitted to fulfill the obligations described above.

1.2 Scope

The feasibility report sets forth the current system of education property tax administration relative to billing and collection, the changes required for State administration of the billing and collection functions, and an analysis of the impacts of that change on the Department of Taxes and other stakeholders. Also, the study explores potential changes to the application of the CLA. The study's scope is informed by a review of relevant legislative history and Tax Department testimony before the House Committee on Ways and Means.

1.3 The Education Property Tax in Vermont

Vermont's state education property tax is a recent development. The Vermont Supreme Court's *Brigham*[2] decision required the legislature to address persistent educational inequality among school districts. In 1997, Act 60 created a statewide education property tax as a mechanism to comply with *Brigham* and provide every town equal opportunity to fund its

2 *Brigham v. State*; 166 Vt. 246 (1997)

schools. The legislature has amended Act 60 during subsequent years, including significant changes in 2003 through Act 68.

Acts 60 and 68 fundamentally changed the relationship between towns, school districts, property owners and the State in regards to education finance. The law also provided an avenue for certain property owners to pay school taxes based on their income.

Changed Relationship

Local property taxes have existed for centuries in Vermont. Local jurisdictions used property tax revenue to cover municipal expenditures, including schools. Act 60 changed the status quo in two important ways. First, the State imposed a tax on property separate from local levies. Second, the statewide tax removed the ability of local jurisdictions to tax directly for education. Despite this fundamental change, the appearance of the process remains consistent with the municipal property tax.

The new statewide education property tax built upon the mechanics of the existing local property tax system. Property valuation remained a local function, as does billing and collection. Accordingly, property owners continue to receive municipal and state property tax bills from the municipality. Local jurisdictions issue the bills, and property owners remit both municipal tax and State education tax payments to municipalities. While education spending levels are voted locally, the State sets the base education tax rate for all property--homesteads and non-residential.

Property Tax Adjustment

Traditionally, a property owner's tax was based on the product of their property value multiplied by the tax rate set by the town. In 1970, the State enacted a rebate program that capped the amount of property taxes due from property owners with household income below a prescribed amount.[3] Act 60 and subsequent laws changed and expanded the income-based limit on property taxes significantly. Qualifying homestead owners may pay their statewide education property tax based on income if the tax due based on income is less than what it is based on property value. Property tax adjustments are currently available to homeowners with household income up to $97,000. For homestead owners with household income of $47,000 or below, an additional adjustment is available which includes municipal taxes in the calculation. The Department of Taxes provides information to local jurisdictions, which they use to adjust property tax bills to credit the property tax adjustment amount.

Education Funding Process

Overall, the Present Act 60/68 system features four major steps in the school funding process:

- School district voters approve a school budget, which determines the per-pupil education spending for each district.
- The State sets the base homestead tax rate, which is adjusted by local education spending, and the nonresidential tax rate; as well as the applicable income percentage for calculation of the property tax adjustment.
- Towns issue bills to all property owners for both municipal and education taxes. For qualifying residents, the bill is adjusted to reflect education tax liability based on household income.
- Money used to fund Vermont schools is transferred to each school district from local jurisdictions and the State based on the education spending approved by voters. The Department of Education guides towns through the transfer process, as local jurisdictions settle up with local school districts and the State.

The feasibility report focuses on steps three and four, the billing and collection of school taxes and transfer of education funds to Vermont's schools. The next section of the report describes the current allocation of billing and collection functions between the State and local jurisdictions.

3 The income level has varied over the years and was compared to total property taxes.

2.0 Current System

2.1 Billing and Collection of the Statewide Education Property Tax

Titles 32 and 16 of the Vermont Statutes provide a framework for state and local officials to administer the education property tax. Overall, administration of the education property tax can be grouped into four categories, assessment functions, tax functions, payment functions, and delinquency functions. Each step is listed below with the responsibility attributed to either local jurisdictions or state government.

Assessment Function

- Identification of property to be appraised as of assessment date (local)
- Appraise property (local)
- Notify owners of value/issue Change of Assessment notices (local)
- Hold grievances and notify grievants of results (local)
- Lodge grand list with town clerks (local)
- Track and maintain homestead and property tax adjustment status (local)
- Advise local assessment officials on issues of assessment and tax administration (state)

Tax Function

- CLA[4] is applied and local jurisdictions notified of education tax rates to be levied (state)
- Tax bills issued based on local grand list value and state rates for the education property tax and the local grand list and municipal tax rate for the municipal portion of the property tax (local)
- State education property tax and municipal property tax collected (local)

Payment Function

- The State Department of Education and Department of Taxes assist local jurisdictions in reconciling the revenue accounting between municipalities, school

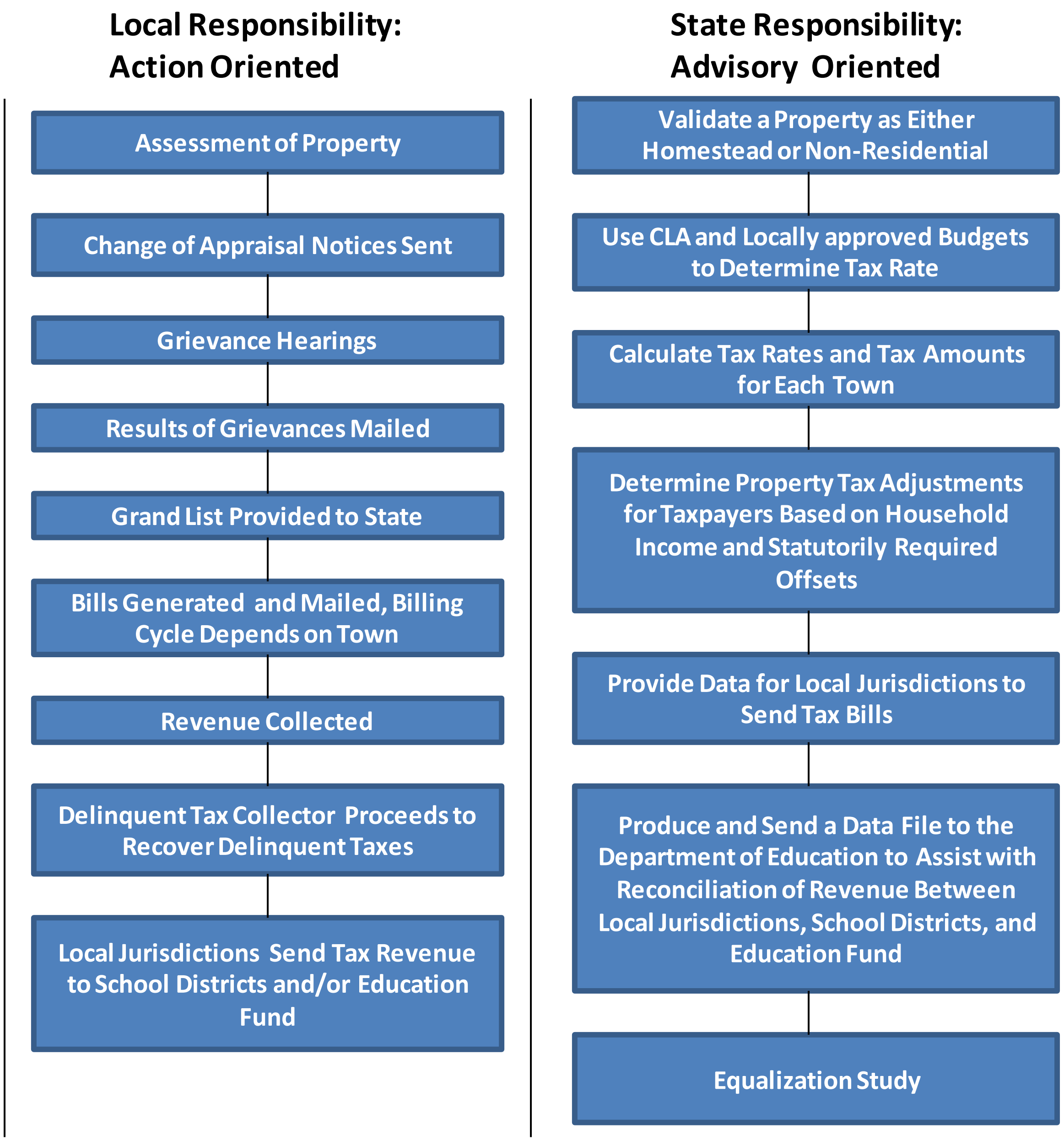
4 Embedded within property tax rates is the CLA, Common Level of Appraisal. The CLA is the ratio of the local assessed values to the state's estimate of fair market value for that municipality. The Tax Department uses the CLA to equalize the education tax rates ensuring equal treatment across towns.

districts, and the State as some towns collect more education tax than their local districts require in education funding, while some towns collect less (state)

Delinquency Functions

- Taxes become delinquent when a taxpayer fails to pay the taxes on the due dates specified on the tax bill. That date must be at least 30 days after the tax bill has been mailed. (local)
- Within 15 days after the tax due date, or a shorter time if the municipality has so voted, the treasurer must issue a warrant and a copy of the tax bill to the delinquent tax collector against the delinquent taxpayers in the amount that remains unpaid. (local)
- The delinquent tax collector may use one of four methods available to collect delinquent taxes, Foreclosure, Distraint, Action at Law (Civil Action), and Tax Sale. The Collector of Delinquent Taxes may choose to accept a payment plan or may choose to take no action at all. The local Board of Tax Abatement may abate taxes under specific circumstances. A lien attaches to the property automatically upon the lodging of the grand list by listers. (local)
- The collector must file a certified annual report with the treasurer and auditors on or before January 15, showing all the delinquent taxpayers as of December 31st, amounts due and years in which taxes were due. (local)

The chart on the next page illustrates the division of labor, demonstrating how the operation of billing and collection remains a local matter with the State playing an advisory role.



The current statutory framework and division of labor builds upon the traditional local property tax. The State has an advisory role with respect to listing practices and provides towns with the data necessary to bill the tax. Specifically, the Tax Department provides municipalities with the tax rate and property tax adjustment amount which is netted against the education tax on the tax bill. Taxes are levied and collected, and local jurisdictions, school districts, and the State settle up financially over the course of the fiscal year. In recognition of the partnership between the State and local municipalities in administering the education tax, local jurisdictions are allowed to retain a statutorily prescribed portion of the tax, valued at approximately $2.05 million in FY 2010.[5]

2.2 Present State of the Administration of Property Tax Adjustments

A description of the present system is incomplete without a review of the process used to determine eligibility for and calculation of property tax adjustments for qualifying homesteads. Administering property tax adjustments based on income requires considerable staff time from the department's Property Valuation and Review, IT, Taxpayer Services, Compliance, and Revenue Processing divisions. Currently, property tax adjustments affect 33 percent of all properties in Vermont and 65 percent of all primary residences.

Property tax adjustments and renter rebates are calculated using Household Income, a measure distinct from Federal Adjusted Gross Income or Vermont Taxable Income for individual income tax purposes. Separate income definitions and calculations require different forms and processing, distinct customer service, a separate technology module within the computer system, and dedicated compliance staff to match the free-standing income definition to federal and state return information to verify accuracy. Approximately 140,000 households file for property tax adjustments totaling about $150 million. A breakdown of responsibilities and resources by division within the Tax Department follows.

Property Valuation and Review

PVR plays two critical roles in administering the education property tax. First, PVR serves as the information liaison regarding property tax adjustments with local jurisdictions. Second, PVR calculates tax rates and tax amounts for each town annually. PVR works closely

5 An additional $3.2 million was distributed to assist local jurisdictions with property assessment in FY 2010. The study does not include a review of state appraisal of property. Therefore, the study does not contemplate redirecting this revenue stream from local jurisdictions to the State; however, this is another potential revenue stream to fund State billing and collection.

with the IT division to assist local jurisdictions. These responsibilities relevant to property tax adjustments require the equivalent of 2 full time employees.

Information Technology Division

Currently, IT plays two important roles in facilitating the property tax adjustment process. First, IT maintains the information for property tax assessments in the Department's Vermont Integrated Revenue Collections System (VIRCS) computer system. Second, IT works collaboratively with PVR , the Department of Education, and Vermont's cities and towns to ensure that local jurisdictions have the information necessary to adjust tax bills and collect the proper amounts. Specifically, IT takes the following collaborative steps to assist local jurisdictions:

1. Provides helpdesk assistance to the towns in their use of the NEMRC and CAMA systems used in the billing and appraisal process
2. Sends Vermont's municipalities an electronic file validating homestead status by SPAN[6] number
3. Loads tax rates and tax amounts calculated by PVR into computer system based on municipally approved budget and education tax rate determined by CLA
4. Runs the offset process for property tax adjustments. The Tax Department is authorized by law to offset property adjustment amounts against other liabilities owed the State, such as unpaid taxes, court restitution, and child support
5. Creates data files for each local jurisdiction with property tax adjustment listed by SPAN
6. Generates and mails letters to all property owners that file property tax adjustment claims, 139,481 total in 2010
7. Produces and sends files to local jurisdictions for traditional municipal property tax rebate program
8. Provides a spreadsheet to Finance & Management to have electronic municipal property tax rebate payments sent out in July and September
9. Produces and sends a data file to the Department of Education with the dollar amounts to be applied to tax bills by town so that they may advise local jurisdictions on the amount of tax revenue to direct to specific school districts and the Education Fund if necessary

6 The SPAN is a unique identification number assigned by the town for each parcel.

The steps listed on the previous page occur annually and require the following IT staff from the Tax Department:

- Equivalent of 1.5 FTE, analysis and systems development
- Equivalent of 1.75 FTE, Technology Help Desk

Taxpayer Services Division

The Taxpayer Services Division provides customer support within the Tax Department. Recently, the Department conducted an analysis of the customer service workflow handled by this division by tax type. The analysis is part of the Department's broader effort to better understand workflow and customer needs and use this information to provide outstanding service. From January 1, 2011 through May 6, 2011, the bulk of the tax season, the income tax section responded to:

- 40,589 Phone calls[7]
- 2,152 Emails
- 20,500 Pieces of correspondence
- 400 Walk-in taxpayers
- 203 walk-ins in the department's satellite desk at the Burlington IRS

The Tax Department estimates that the majority of inquiries handled by the Income Tax Section staff arise from property tax adjustments and rebates. Currently, the Department is keeping more detailed correspondence logs to drill down beyond correspondence volume to subject matter. The Department will likely have better data in 2012.

The Taxpayer Services division employs 13 FTEs in the income tax section. It is estimated that the equivalent of 4-5 FTEs are required to administer property tax adjustments.

Compliance Division

The Compliance Division performs the classic audit function for the Tax Department, collecting unpaid bills and ensuring the integrity of the tax laws. Currently, the equivalent of 2

7 This number does not include direct calls to individual tax examiners.

FTEs audit property tax adjustments. Specifically, staff examines the school property claims filed by taxpayers according to departmental standards and bills back inappropriate claims. Typically, inappropriate property tax adjustment claims are discovered as a result of comparing Household Income schedules to federal and state income tax returns. Corrections to the Household Income calculation change the school property adjustment amount, typically reducing that amount.[8] These efforts have yielded the following assessments (amount billed, not collected) including interest and the maximum penalty of 10%:

- **Fiscal Year Ending 2010:**
  - 1780 bill backs leading to assessments of $904,623.66

- **Fiscal Year Ending 2011**
  - 2483 bill backs resulting in assessments of $1,630,676.20[9]

These noncompliance rates are consistent with personal income tax, trust taxes, and corporate income taxes rates. Largely, the adjustments are done as post audits when the information for comparison becomes available.

Revenue Processing Division

The Tax Department's Revenue Processing Division processes all forms related to property tax adjustments, including the Homestead Declaration, Withdrawal of Homestead Declaration, the Household Income Schedule, and Property Tax Adjustment Claim. 160,000 Vermont households file some combination of these forms annually, with the exact number of forms varying each year. These forms arrive in spring, concurrent with the Personal Income Tax filing season. The seasonal aspect of this work requires the employment of temporary employees. The Department has determined that approximately 2 full time temporary

8 Compliance issues are driven by the difference between income for federal and state income tax purposes and the calculation of Household Income found on HI-144, the Household Income Schedule. Many HI-144 filers have no requirement to file an income tax return. Others misperceive the differences between income for income tax purposes and income for Household Income/Property Tax Adjustment purposes.

9 Increased numbers should not be perceived as increasing problems in the program. Rather, the Tax Department conducted a review of previous years that yielded increased assessments. The urgency to review past years arises, in part, from the three year statute of limitations on property tax adjustments.

employees are deployed to process forms and correspondence related to property tax adjustment claims.

Summary of Resources Required for Property Tax Adjustment Claims

The previous sub-sections set forth the current level of resources required to administer property tax adjustment claims. They are summarized in the table below. The study will examine ways, if any, that the responsibilities and resources required for state billing and collection would affect the current level of service required to administer property tax adjustments.

Current Staff Resources Required for Property Tax Adjustment Program

2 Revenue Processing Temporary FTEs, (Process Documents and Payments)	3.25 Information Technology FTEs, (Analyst, Developer, and Help Desk)	2 PVR FTEs
4-5 Taxpayer Services FTEs, (Customer Service)	2 Compliance FTEs, Compliance Officers (Delinquencies)	1 Legal FTE

2.3 Present State of Technology and Technology Priorities at the Department of Taxes

Increasingly, technology defines the scope and speed of public sector challenges. The Department of Taxes and this feasibility study offer a compelling example of the complex interplay between policy priorities and technology capabilities. The feasibility study must be understood in the context of the Department’s current technology capabilities and future technology priorities. Present capabilities can be a limiting factor on the speed of policy implementation. Future priorities can both inform the order in which change occurs and demonstrate the opportunity cost of evolving priorities. A brief description of the Department’s current and future priorities provides the background by which to understand how shifting the responsibility for billing and collection of the education property tax would impact the department.

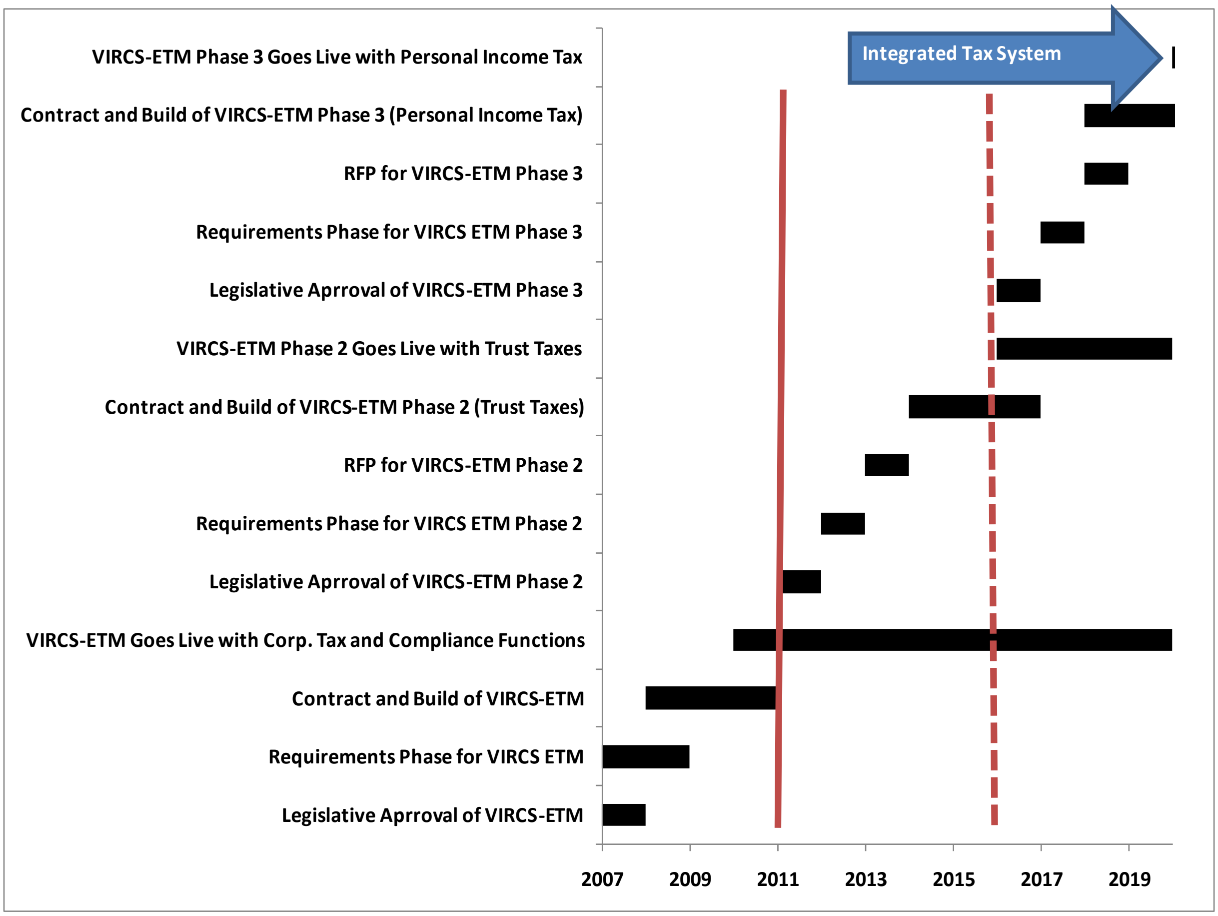
The Department of Taxes is in the midst of a profound technology transformation. Specifically, the Department, at the legislature's direction, has committed to creating an integrated tax processing platform, the Vermont Integrated Revenue Collections System-Enterprise Tax Management (VIRCS-ETM). VIRCS-ETM is designed to replace the multiple computer systems now used to administer taxes, eliminating a siloed approach that requires complex interfaces between computer systems of different generations.

The Department of Taxes is moving toward VIRCS-ETM presently. The Legislature approved the creation of VIRCS-ETM in §282 of Act 65 (the Big Bill) of 2007. The project is designed to be implemented in stages. Phase 1 was completed in October 2010. The Legislature approved the work necessary to prepare for and begin Phase 2 in §C103.1 of Act 63 (the Big Bill) of 2011. The Department has the direction and funding to make substantial progress on Phase Two under current law; however, the final cost and timeframe will not be set until after the submission and review of bids to an RFP scheduled to be released in 2013. The next figures depict the historical progression of the Department's computer systems and the proposed timeline for the VIRCS-ETM project.

Progression of Technology at the Tax Department, from Paper to Silos to Integration

Year	Computer Systems			
Prior to 1980	All Manual Processing			
1980	**Mainframe:** trust taxes, corporate income, personal income, and collection	All other taxes processed manually		
1998	**VIRCS**: Trust taxes	**Mainframe**: corporate income and personal income	**CACS-G**: Collections	All other taxes processed manually
2001	**VIRCS**: Trust taxes, personal income tax, property tax adjustments	**Mainframe**: corporate income	**CACS-G**: Collections	All other taxes processed manually
2009	**VIRCS-ETM**: Corporate Income, Collections, Several smaller taxes	**VIRCS**: Trust taxes, personal income tax, property tax adjustments	All other taxes processed manually	
Proposed Future State	All taxes in VIRCS-ETM			

Proposed VIRCS-ETM Project Timeline, Phases 1, 2, 3



The solid line indicates that the Department has completed Phase One of this project. The dotted line indicates that the Legislature has approved the steps necessary to begin Phase 2. The proposed design and implementation of future phases is subject to ongoing analysis and evaluation.

Beyond VIRCS-ETM, the Department is working on a slate of other technology projects. These projects represent the Department's current strategic priorities alongside VIRCS-ETM development, and they are a combination of department driven and legislative projects each designed to facilitate taxpayer interaction with the Tax Department and improve departmental efficiency. The timeline for these priorities extends over the next several years, with estimated start dates listed:

- **Business Registration Portal:** The Department of Taxes is engaged in a partnership with the Department of Information and Innovation, Agency of Administration, Secretary of State, and Agency of Commerce and Community Development to create a business portal that will provide Vermont's potential businesses a single web site to register with the State. This would eliminate the need for entrepreneurs to interact with multiple state agencies when forming a business. Project began June of 2011.

- **VT Pay Upgrade:** The Department is working with DII and the Vermont Information Consortium (VIC) to enhance the VT Pay web site. The project would allow taxpayers to pay their current income tax payments, estimated personal income tax payments and bills using ACH debit and ACH credit. The site currently allows payment only by credit card which significantly restricts utilization of the site as taxpayers are charged fees to pay their taxes. Also, the Department is working to expand VT Pay to allow taxpayers who owe the Department money to sign up and create payment plans on-line. Business case and requirements work submitted to DII and VIC July of 2011.

- **E- Current Use:** §§ 33-35 of Act 45 of 2011 mandated the transition of the Use Value Appraisal Program (Current Use) to electronic administration. The preferential rate for land enrolled in use value appraisal was repealed so the general rate of 1.25 percent applies. The amount of property transfer tax revenue allocated to PVR is increased from 1 to 2 percent for 5 years with the increased revenue to be used to fund the transition. Business case and requirements work submitted to DII and VIC July of 2011.

- **Web Site Upgrade:** Based on legislative input, the Department of Taxes is reevaluating its outreach to taxpayers. One major goal of this effort is a redesigned web site featuring clear content and enhanced functionality that better meets taxpayer needs and conforms to modern best practices. The Tax Department has convened a working group across divisions and partnered with the Department of Information and Innovation (DII) to address this technology challenge. Department wide project began May of 2011. Estimated completion prior to 2012.

- **W2 Enhancement:** Recently, the Department of Taxes created the ability for payroll companies and certain other qualifying employers to electronically submit W2 files, 1099 information files, and Annual Reconciliation of Withholding Tax Account (Form WH-434). Based on the excellent results of this project, the Department is working to offer enhanced electronic services pertaining to employee payrolls. For example, the Department is working with VIC to develop an online data entry W-2 system that would allow small businesses to directly enter the W-2 information for each employee online. This would offer taxpayers with smaller payrolls the ability to data enter both their Annual Reconciliations (Form WH-434) and their annual W-2s. The system offers improved functionality for taxpayers and processing efficiency for the Tax Department. Phase 1 completed in 2010. Business case and requirements work for Phase 2 submitted to DII and VIC in June of 2011.

- **Modernized E-File:** The IRS is requiring the Department of Taxes to adopt and implement a new e-file system for personal income taxes. Among other changes, Modernized E-File will transition the technology architecture to industry standard practices for identifying, storing and transmitting data rather than the proprietary data transmission formats used by older e-file programs. The Vermont Department of Taxes must adopt Modernized E-File in the next 2 years or it will lose the ability to offer taxpayers and tax practitioners electronic filing of Personal Income Tax returns. Project estimated to begin Fall of 2011.

- **Business E-Filing:** The Tax Department does not offer electronic filing of corporate tax returns. The Department of Taxes believes that this enhancement would offer benefits and efficiency for taxpayers and the Department. Project start date to be determined.

- **Data Warehouse:** The Department's data warehouse project involves leveraging multiple data streams and cutting edge software technology, software tools, and industry best compliance strategies to narrow the tax gap and maintain the integrity of the tax laws more efficiently. The project began in May of 2011, and it will continue for the next five years yielding software tools, best practices, and knowledge transfer to employees across most divisions. Also, the project is benefits based with proceeds paying for the project itself and the immediate next steps of Phase 2 of VIRCS-ETM. The remainder contributes directly to the General Fund.

The policy choice to create State responsibility for the billing and collection of the education property tax would affect the implementation of these priorities. Likewise, the Department's current state of technology capability affects its ability to assume responsibility for billing and collection. The study will examine how technology capabilities and current and future policy priorities affect the feasibility and implementation of State billing and collection.

The next section of the study examines those aspects of the system now performed by local jurisdictions that the State would administer to bill and collect the education property tax.

3.0 PROPOSED SYSTEM

3.1 Description of Proposed System

The proposed system analysis revisits the assessment function, tax function, payment function and delinquency function. Each section includes an analysis of policy changes and resources necessary to implement State billing and collection. The section concludes with a summary of requirements and resources to implement change and an estimated timeline for implementation.

Assessment Functions

State billing and collection of the education property tax would change the assessment function in three ways. First, the State would adjust the calendar of assessment activities to ensure efficient billing. Second, the State will need some incentive to ensure local jurisdictions complete their work in time for State to levy and collect taxes in timely manner. Third, local jurisdictions and the State would need to work closely to track ongoing changes due to appeals, or changes made under errors and omissions. The latter relates to such things as changes to the classification of a parcel due to the late-filing of a homestead declaration, changes made by the listers due to an obvious error they made, such as failing to add the value of a new house that was built. Such ongoing changes will require the continuing transfer of data to the State from the Town. Such changes will trigger corrected tax bills and/or credits.

Calendar of Assessment Activities

State billing and collection depends upon the lodging of the grand list. Any delay in lodging the grand list would adversely impact the State's ability to calculate and send bills and delay the timing of payments to the Education Fund. These delays would require the State to either borrow money to cover the shortfall or delay payment to school districts. Therefore, the grand list would need to be completed and in State's hands much earlier than present law provides. This would require a change of the assessment date from April 1 to January 1 and changes to the related statute sections. A comparison of current and proposed assessment activities calendars is below:

Current Assessment Calendar[10]	Proposed Assessment Calendar
April 1 Assessment Date	Jan 1 Assessment Date
June 4 Change of Appraisal Notices sent	April 1 Change of Appraisal Notices sent
June 19 Grievance hearings begin	April 15 Grievance hearings begin
July 2 Grievance hearings end	May 15 Grievance hearings end
July 9 Results of grievances mailed	May 25 Results of grievances mailed
August 15 Grand list provided to State	May 25 Grand list provided to State
July 15 First tax bills mailed	July 15 First tax bills mailed

Ensuring Timely Completion of the Grand List

Current law requires the grand list to be lodged with each town clerk on July 9. Towns are required to provide the grand list to the State by August 15. Local jurisdictions that do not provide the State with the grand list by this date may be subject to the withholding of all State payments until such time as the proper filing is completed. The Department has been reluctant to put that sanction into place, choosing to rely on the cooperation of the towns. Most file within a few weeks of the August 15 date.

Tracking Ongoing Changes

Tax bills can change during any given year due to a variety of factors, e.g. appeals, errors and omissions changes. Typically local jurisdictions make these changes to the grand list and adjust tax bills accordingly. The State would need to collect this information in a timely manner so that it may send accurate bills or amended bills where necessary. Taxpayer

10 The Assessment activity calendar is slightly different for towns depending on whether they have a population greater than 5,000.

Services would likely facilitate this relationship with local jurisdictions and work with IT staff to ensure that records, bills, and collection notices were changed accurately in a timely manner.

The legislative history of this study and subsequent testimony leads to the conclusion that statewide appraisal of property is not within the intended scope of this study. The lack of exploration of this issue should not be viewed as endorsement or opposition of the statewide appraisal concept. Specifically, state billing and collection of the education property tax does not require the statewide appraisal of property. Local listers could continue to value properties for municipal tax assessments, and the State would continue to use the grand list lodged by the listers. The State would continue to use the same analytical tools, the equalization study and CLA, to adjust the grand list values to ensure equal tax treatment across local jurisdictions.

Tax Function

State billing and collection of the property tax alters the tax function. Local jurisdictions would remove information regarding the education property tax from the municipal tax bill. Also, local jurisdictions would no longer collect, deposit, or transfer the tax revenue generated by the statewide property tax. Instead, the State would need to create the capacity to issue bills and collect the tax independent of local jurisdictions. Building this capacity requires expanding the Tax Department's computer systems, tax return and revenue processing, and customer service. This expansion generates costs in three broad categories:

1. Technology Resources: design and implementation of a computer system to bill and collect the education property tax,
2. One-Time and Ongoing Personnel Costs: the people required to perform the new functions and the space and materials they require,
3. One-Time and Ongoing Processing Costs: the resources needed to process the tax bills, returns and related notices.

Each resource is described in the following sub-sections.

Technology Resources

The threshold question, like so many others now in government, is how to build and maintain the technology architecture for this particular function. The Department could create property tax bills in one of two ways. First, the Department could contract to purchase an enterprise tax system to manage property tax billing. Second, the Department could integrate property tax billing into VIRCS-ETM, the Department's anticipated integrated tax system currently under development. [11]

Contracting for a Solution

Multiple corporations offer property tax software solutions, including computer assisted appraisal, land record management, billing, and collection modules. The State could contract with a vendor for billing services, while the Department would rely upon its own collection systems. The State would manage this relationship by providing the contractor with the grand list data created by the towns and the property tax adjustment data supplied by the Tax Department. The primary resource need in contracting for a solution would be an appropriation to fund the contract, personnel, either contract or internal, to maintain the system and its interfaces over time, and future dollars to fund technology hardware replacements and upgrades.

The State would have two likely contract partners to develop a system for state billing of the education property tax. First, the state could contract with the New England Municipal Resource Center (NEMRC). NEMRC is a Vermont based company that provides billing services for all 246 local jurisdictions, creating, printing, and mailing the approximately 320,000 local property bills. Second, the State could contract with one of several national firms that offer property tax software solutions.

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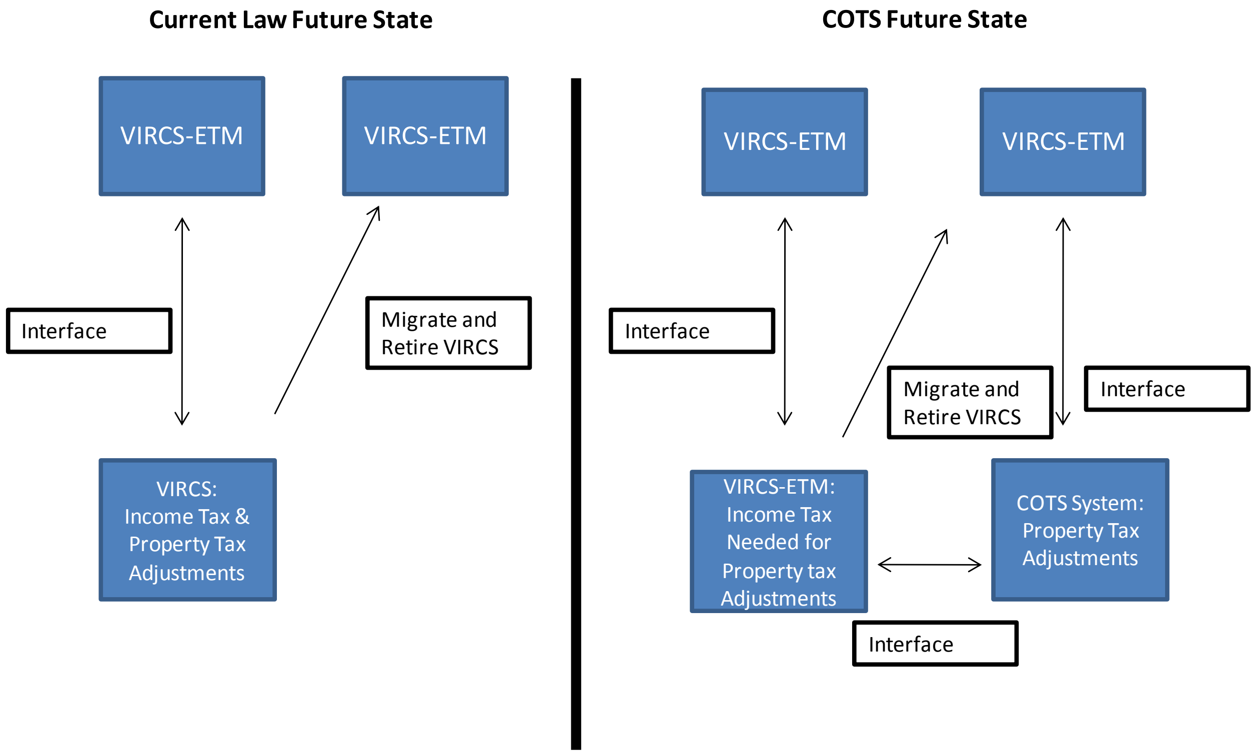
11 The Department would continue to use VIRCS-ETM for collections under either scenario.

A State contract with NEMRC would have several built in advantages. NEMRC is familiar with Vermont's education tax and has preexisting relationship with the State and local jurisdictions. Also, Department analysis indicates that NEMRC would likely offer the most cost effective alternative. The initial estimate for a NEMRC software solution to the State for billing is approximately $1 million. Ongoing costs in out years are to be determined. NEMRC billing for the State would be an increase in the scale of their operation in Vermont as the State will send as many bills as all local jurisdictions combined, and the state has 33 times the number of parcels as Burlington, the next largest jurisdiction.

An analysis of recent contracts by public agencies for property tax software solutions reveals a broad range of functionality and price. Jurisdictions are purchasing enterprise software solutions for property tax appraisal, land use management, billing, and collection or some combination thereof. These contracts provide a rough cost estimate for Vermont. The closest comparable contract for a software solution for billing would suggest an estimated minimum cost of $3,000,000. This price estimate does not include post contract costs for software and hardware service and maintenance.

Another cost, though more difficult to quantify at present, is the cost of building interfaces between a commercial off the shelf (COTS) tax software system and the Tax Department's custom tax systems. A COTS product would be a stand alone, siloed computer system. It would not be part of the integrated tax management computer system currently under construction. Therefore, the Department would be required to build a custom interface between the COTS system and the income tax computer system for the purposes of property tax adjustments. Furthermore, the process would be done twice: once for an interface between the COTS system and VIRCS and again when VIRCS is retired and the Household Income data migrates to VIRCS-ETM. Interface construction is complex, and it requires IT staff resources that cannot then be deployed to other projects. The figure on the next page illustrates the potential additional work involved in implementing a contract solution.

Technology Interfaces: Integrated System Versus a COTS System



Building Property Tax Bills into ETM, the Department's Integrated Tax Management System

The Department's current technology priority plan anticipates moving all tax types into VIRCS-ETM. Accordingly, the Department could contract to build a custom VIRCS-ETM module for billing of the property tax. Department research and analysis would set forth the following path to build a property tax module for VIRCS-ETM:

- Department of Taxes internal process to define requirements for education property tax system in order to create and facilitate the Request for Proposal (RFP) to add a property tax module to VIRCS-ETM[12]
    - Six month process with estimated cost of $250,000

12 The Department of Taxes would expect the property tax module in VIRCS-ETM to offer the same level of functionality as other taxes, including interfaces with the state VISION system to deposit money into the Education Fund, the revenue accounting system with additional capabilities to sort taxpayers for statistical purposes (e.g., homestead/nonresidential), and the current VIRCS system for income tax to net our property tax adjustments and offset liabilities with other taxes among other functions. Also, the Department would expect to offer taxpayers the same functionality. For example, real time tax information would need to be available to real estate professionals.

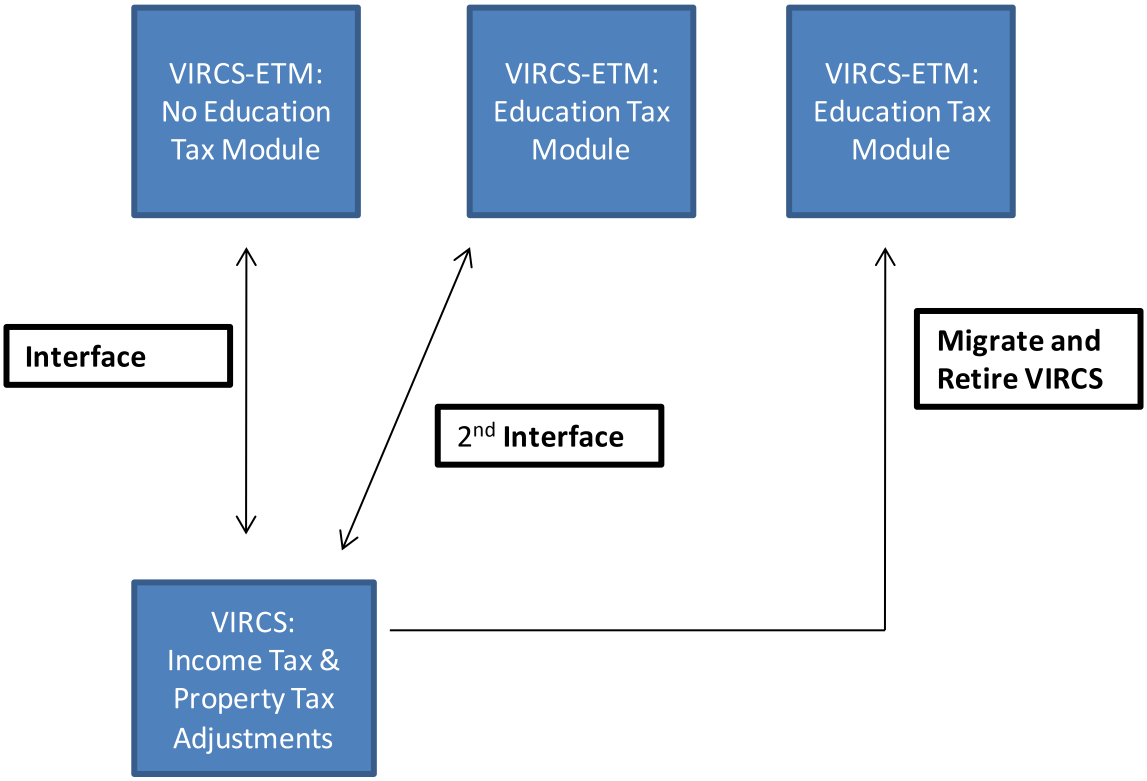
- Issue RFP and evaluate submissions[13]
  - Bidding and evaluation process is a three month process beginning after completion of proposal document
- Partner with contractor to build VIRCS-ETM property tax module
  - Twenty four month process
  - Estimated cost is $3,000,000. Cost estimate is based roughly on the cost of the present VIRCS-ETM system. It is assumed that the property tax module will be much less complex than the current tax systems; however, there are five times as many property tax parcels than current VIRCS-ETM tax filers. True cost would be determined during the RFP process.

Overall, the Tax Department envisions a 33 month technology process that costs approximately $3.25 million to build a custom property tax module into VIRCS-ETM.

The advantage of creating an add-on module in VIRCS-ETM is that it furthers the goal of having a single, integrated tax system. Also, there is the potential to avoid the need for custom interfaces or support of multiple systems once all taxes are migrated from VIRCS to VIRCS-ETM. This potential efficiency would only occur if the property tax model was built simultaneously with the migration of income taxes from VIRCS to VIRCS-ETM or after this migration. Otherwise, the Department would need to build and maintain a custom interface between the property tax VIRCS-ETM module and income tax system in VIRCS for property tax adjustments until such time as VIRCS is retired and its data migrated into VIRCS-ETM. Personal Income Tax migration into VIRCS-ETM is tentatively scheduled to be completed in 2016. The additional step required if the property tax is added to VIRCS-ETM prior to the income tax components is set forth in the figure on the next page.

13 VIRCS-ETM is a cutting edge Oracle based product, and the Department of Taxes believes there are a very limited number of vendors with enough familiarity with the system to design an education tax billing system as an add-on.

VIRCS-ETM Module Future State:
State Billing and Collection
Mandated Immediately



The Department views either the use of a COTS system through a vendor or a custom property tax module built into VIRCS-ETM as feasible. The decision points are price, given the potential difference between NEMRC, another outside vendor, and an add-on module to VIRCS-ETM, and the importance of developing an integrated tax processing platform. COTS software solutions are viewed as easier to implement while a single integrated tax system would allow professionals throughout the department to conduct business seamlessly without siloed functions or expertise.

One Time and Ongoing Personnel Costs

The Department would expect to offer the same level of functionality and service for the property tax as any other tax. Accordingly, the Tax Department would need to add the additional personnel necessary to handle property tax returns, answer taxpayer questions, provide an accounting for the increased revenue, service the technology, and ensure taxpayers comply with the law. These costs are estimated by the Tax Department by comparing the volume of the education tax to other taxes and extrapolating based on the relevant ratios based on current service levels. The education tax accounts for just over $900 million dollars annually. All other taxes collected by the department total approximately $1.2 billion annually. The personnel resources and accompanying costs are set forth below by division. These employees would create both a one-time start up cost and ongoing expense for the Tax Department.

4 Revenue Processing FTEs, (Process Documents and Payments and Perform Revenue Accounting)	2 Information Technology FTEs, (Development, Quality Assurance, Business Analysis, and Support)	3 Property Valuation and Review FTEs (Service for the Towns and Real Estate Transactions)
5 Taxpayer Services FTEs, Examiners (Customer Service)	18 Compliance FTEs, Compliance Officers (Delinquencies)	2 Legal FTEs, Compliance Attorneys (Delinquencies & Legal Challenges)

The Tax Department estimates the initial annual cost at $2,428,000. This is based on a total of 34 new employees times $60,000 annual salary including benefits, totaling $2,040,000. Next, the Department adds 20 percent of each salary for annual operating support associated with 34 employees for a total of $408,000.

Space to house these employees is another potential ongoing cost. The Department could accommodate additional hires; however, it is unclear whether the Department could absorb 34 new employees in its current space. On average, employees require 81 square feet, and State office space rents for $13.82 per square foot. Accordingly, the Department may incur an additional $35,821 annually in leasing costs.

Additional onetime costs include both technology and office furniture, such as desks, chairs, files, and telephones for 34 new employees. The costs are listed on the next page.

- 34 computers workstations are estimated to cost $27,000
- Office furniture for 34 employees is estimated to cost $45,600

New employee costs would be substantial with the implementation of State billing and collection, and it is unlikely that current staff could absorb these duties given current employment levels due to recent layoffs and attrition due to the hiring freeze.

One Time and Ongoing *Processing Costs*

The Department can estimate with some accuracy the cost of processing approximately 320,000 education property tax bills. The only foreseeable one-time cost is a new scanner to ensure that property tax bills and all other tax bills be continued to be processed, and checks cashed, in a timely manner. The estimated cost of this equipment is $250,000. This cost is based on the recent purchase of two similar scanners.

Relevant ongoing costs include the printing and mailing of bills and the printing and mailing of delinquency notices. These costs are estimated below based on the current cost to the Tax Department of printing and sending similar correspondence.

- Estimated cost to print bills is $28,444 ($.08 per bill X320,000 bills)
- Estimated cost to mail bills is $99,200 ($.031 per bill X 320,000 bills)
- Estimated cost to print delinquency notices is $2,844 ($.08 per notice X32,000 notices)
- Estimated cost to mail delinquency notices is $9,920 ($.031 per bill X 32,000 bills)

The estimated first year cost of printing and mailing bills would be $390,408, with the processing costs diminishing by $250,000 in out years. The cost may diminish in out years as the Tax Department and taxpayers migrate toward electronic billing and paying options.

Payment Function

The payment function would change if the State were responsible for billing and collection of the education property tax. The Department of Education would no longer manage the flow of revenue between sending and receiving local jurisdictions, school districts, and the

State. Instead, all education tax revenue would flow directly to the Department of Taxes, and the Tax Department would transfer all tax revenue to the Education Fund. The Department of Education would send funds out to each schools district. This eliminates local jurisdictions from the collection, holding, and distribution of education tax dollars.

The major requirement for the Tax Department would be the creation of an interface between the Department's revenue processing system and the State VISION system to allow the direction of revenue into the Education Fund. The work to create and maintain this interface is undetermined; however, it is not considered an obstacle to the feasibility of State billing and collection.

Another issue arising within the payment function is the timing of education payments. Currently, municipalities set their own dates for tax bills and payments. State billing and collection would require the State to set its own property tax billing and collection cycle. These dates will not be synchronous with local jurisdictions as town billing dates are not uniform.

Delinquency Functions[14]

Currently, the State plays no role in education property tax delinquencies. State billing and collection would require the State to act when property owners fail to pay the education property tax. The introduction of State compliance activities alongside local delinquency collection efforts creates five challenges involving liens, off-sets, abatements, late payments, and cultural changes with the Tax Department's Compliance Division.

14 The one-time and ongoing personnel costs for delinquency through the Department's Compliance Division was set forth above with all other personnel costs for the sake of clarity. This delinquency section focuses on other related delinquency/compliance challenges.

State Property Tax Liens

No policy exists providing a State education property tax lien. Policymakers would need to decide whether the State should be given an automatic lien and tax sale powers. Towns currently have these powers with respect to the education property tax. If a lien arises, the legislature would need to determine whether the lien was superior or subordinate to the lien for municipal property taxes. Currently, authority to conduct tax sales for delinquent property taxes is reserved to municipalities. If the Legislature chooses not to create an automatic lien for education taxes and tax sale authority in the State, it can be expected that delinquencies would exceed their current aggregate level. At a minimum, payment of municipal taxes would be preferred over payment of education taxes.

Tax Offsets

Taxpayers with certain unpaid obligations are subject to offset. An offset applies a taxpayer's refund or payment to unpaid obligations to certain state agencies. Current law provides for a two-tiered offset process. First, the department may apply a refund to the outstanding Vermont state tax liability of a taxpayer, including a taxpayer's liability for interest, penalties, and fees before any portion of a refund is transferred into the offset process for other state agencies. Next, refund amounts are offset against liability to other specified state agencies. During this second process, state law requires that taxpayers with multiple unpaid obligations extinguish the largest obligation first. Introducing the education property tax delinquencies into this process will likely reduce the amount of revenue available for offset to other state agencies, including offsets for child support, restitution to victims of crimes, and court fees. The Legislature could choose to remove the Tax Department's superior offset position; however, the large dollar amounts of education property tax bills make it likely to exhaust many offset claims. Any legislative strategy that would promote offsets of other agencies over the Tax Department may have a deleterious effect on both the General Fund and Education Fund.

Abatement

Presently, the State does not have a property tax abatement program as the authority to abate taxes resides at the local level with boards of abatement. Currently, the Department's abatement authority for taxes within her jurisdiction resides with the Commissioner of Taxes. Accordingly, this duty would fall to the person is this position or another body would need to be created and convened. Estimating the impact of this function is difficult. Costs would depend upon the size of the board, its membership, its location in Montpelier or travelling throughout the state, and the support staff needed at the Tax Department to help the board decide abatement claims.

Late Payments

Currently, local jurisdictions must send all Education Property Tax Revenue to either school districts or the State within 20 days of the due date. An additional 120 days is allowed for delinquencies. Local jurisdictions must pay the State regardless of whether these delinquencies are collected, and local jurisdictions sometimes borrow to meet this obligation. Now, the State would be required to make up that difference.

Cultural Change

The Tax Department's Compliance Division prides itself on working toward common sense solutions that honor the taxpayer's willingness and ability to pay and the integrity of the tax code. Much of this flexibility derives from the wide latitude that current law provides the Tax Department in collecting unpaid taxes. The statutes governing delinquent property taxes are much more prescriptive. The rigidity of the law and volume of property tax filers would require the Department's compliance division to engage in a much more rigid compliance process with taxpayers.

3.2 Estimated Timeline and Decision Points

The estimated timeline and decision points for State responsibility for billing and collection of the education property tax are listed below. The timeline's primary assumption is enactment of state billing and collection during the 2012 legislative session. The timeline would be delayed by a later passage. Also, the amount of time allocated for deploying the technology is a conservative estimate based on departmental experience. The actual timeline would be based on responses to the RFP.

- Spring 2012: Enactment by the Legislature with accompanying appropriation for initial technology costs
  - Policy issues to be resolved through enactment legislation or delegation of authority to the Tax Commissioner include:
    - Changes to the assessment calendar. Specifically, whether to move the assessment date to January 1st to ensure State billing by July
    - Prioritization of liens/automatic lien
    - Prioritization of tax offsets
    - Establishment of State level abatement procedures
    - Permit Tax Department to retain a portion of the education property tax to administer the tax as is done currently by local jurisdictions

- July 2012: State billing and collection becomes law

- July 2012 – December 2012: Tax Department staff works with an outside consultant to develop the technical requirements that form the basis of the RFP

- January 2013 – March 2013: RFP published and bids submitted and reviewed

- April 2013: Vendor signs contract
  - Decision whether to contract for a commercial off the shelf product with NEMRC or different vendor. Most important considerations include cost and whether the Tax Department should build a custom software module that furthers its goal of an integrated tax processing system

- April 2013 – March 2015: Development of the education property tax software
  - Ancillary development of technology systems to allow real time property tax liability search for real estate transactions
  - Ancillary development of interfaces (if necessary) to connect software system with other Tax Department systems. Need for interfaces unnecessary if

education tax is built into VIRCS-ETM concurrently with personal income tax/property tax adjustment data

- September 2014 – March 2015: Recruitment, hiring, and on-boarding of 34 staff members to administer education property tax.
- April 2015: System goes live
- July 2015: First education property tax bills sent

The feasibility study offers a rough estimate of the initial and ongoing costs associated with assuming responsibility for state billing and collection of the education property tax. Also, the feasibility study sets forth the staff necessary to bill and collect the education property tax. The total staff and resources required are set forth the figures below.

New Staff Resources Needed for State Billing and Collection

4 Revenue Processing FTEs, (Process Documents and Payments and Perform Revenue Accounting)	2 Information Technology FTEs, (Development, Quality Assurance, Business Analysis, and Support)	3 Property Valuation and Review FTEs (Service for the Towns and Real Estate Transactions)
5 Taxpayer Services FTEs, Examiners (Customer Service)	18 Compliance FTEs, Compliance Officers (Delinquencies)	2 Legal FTEs, Compliance Attorneys (Delinquencies & Legal Challenges)

Estimated One-Time and Ongoing Costs for State Billing and Collection

Activity	First Year Cost	Minimum Out Year Cost
Technology Development	$1,250,000 - $3,250,000	Unknown [15]
One-Time and Ongoing Personnel Costs	$2,485,021	$2,448,000
One-Time and Ongoing Processing Costs	$390,408	$140,408
Total Costs	$4,125,429 - $6,125,429	$2,588,408

15 Technology systems require ongoing maintenance and hardware upgrades and replacements on a recurring basis. These costs are difficult to estimate without a specific proposal to evaluate. One recent Tax Department contract set aside 6 percent of the contract cost for ongoing maintenance and a hardware refresh after 5 years.

4.0 POTENTIAL IMPACTS

A policy choice to shift responsibility for billing and collection of the education property tax to the State would affect the Tax Department's stakeholders. This section of the report sets out the impact of State billing and collection for each major stakeholder group.

4.1 Impact on Taxpayers

Overall, state billing and collection of the property tax may increase clarity, confidentiality, and redundancies for property owners.

Clarity

Separate bills will make it clear that the education property tax is a State tax. Right now, the consolidated bill and collection led by local jurisdictions may mask the fact that the tax bill is for a State obligation to support education in Vermont. Also, separate billing and collection would raise awareness regarding how much of the tax bill is attributable to the municipal property tax and how much is attributable to education. Clearer linkages may provide voters with a better sense of, and sensitivity to, the growth rate in spending for either municipal or education taxes.

Confidentiality

Homestead property tax bills are public records. Concerns have been raised by taxpayers in the past that the property tax adjustment amount and property tax value could be used to determine the approximate Household Income of a taxpayer. Tax documents issues solely by the Department of Taxes to a taxpayer are confidential. Therefore, education property tax bills issues by the Tax Department to individual taxpayers would likely be confidential as well. This may eliminate any lingering confidentiality concerns.[16]

16 The Attorney General issued an opinion on this issue to the Tax Commissioner and Secretary of State in 2007. See http://www.state.vt.us/tax/pdf.word.excel/pvr/propertyadjattorneygenopinion.pdf.

Redundancies

State billing and collection of the education property tax would create redundancies for taxpayers. Taxpayers would transition from a consolidated local property tax bill to two separate property tax bills. These bills will not be issued or collected at the same time given the variety of billing schedules utilized by local jurisdictions across the State. Therefore, taxpayers will have multiple property tax bills and pay dates.

Property tax customer service questions will now be directed to both local jurisdictions and Montpelier. Right now, taxpayers may contact Montpelier regarding the education property tax, but these questions seem confined to property tax adjustment issues. Rather, many local jurisdictions are offering customer support for both taxes, particularly given the strong history of the municipal property tax and many actions that local jurisdictions take regarding the tax.

Abatement for taxpayers would be required to occur twice, once locally and once at the state level. It is unclear whether this process would occur in Montpelier, regionally, or locally. The additional proceeding will require additional taxpayer time, effort, and resources.

Local variability is another challenge in state billing. For example, towns can and do vote down school budgets. Local jurisdictions sometime offer taxpayers the ability to pay in one, two, or four installments. There can be a discount for early payment. State billing and collection will be different. Differences like these result in one of two general outcomes. The State can choose to harmonize these differences by statute; however, this will lead to reduced local control. Alternatively, the State will permit local variations currently chosen by voters at the local level and make accommodations. These accommodations may increase the complexity and cost of billing and collecting the tax.

Beyond specific redundancies, taxpayers may face systemic redundancies. It is not clear that state billing and collection would create significant efficiencies for the State or local jurisdictions. Any duplication of services or addition of services will ultimately be reflected in the costs of the system and passed on to taxpayers.

4.2 Impact on Local Jurisdictions

State billing and collection removes this obligation from local jurisdictions. This may be considered a matter of fairness as it is a State tax. Yet, it is unclear the extent to which state responsibility for billing and collection may reduce local workloads through increased efficiency. It is difficult to quantify incremental savings from decreased workflow across 246 local jurisdictions, particularly as the appraisal, billing, and collection of the municipal property tax will remain. While efficiency benefits are uncertain, State billing and collection will reduce local revenues. Comparison of how much the State currently pays to local jurisdictions for billing and collecting the tax ($2.05 million) and the estimated annual cost for state administration ($2.588 million) may demonstrate, in part, an underfunded mandate shouldered by local jurisdictions. Yet, no longer receiving the revenue associated with this collection, approximately $900 million, has several significant fiscal implications. Specifically, local jurisdictions may lose certain revenues or incur new costs if the State assumes responsibility for billing and collection of the Education Tax.

Removal of Float

Currently, local jurisdictions collect over $900 million dollars on behalf of the State. These jurisdictions may deposit this tax revenue in the bank until such time as the State requires a transfer to local school districts or the Education Fund. Local jurisdictions benefit from interest accrued. Also, some jurisdictions use this money to smooth over cash flow issues, eliminating the need to go to the market to borrow. The removal of these funds would reduce revenues for local jurisdictions and potentially raise costs. Conversely, the State would benefit from the float.

Removal of the Statutorily Prescribed Fee

Current law sets the fee that local jurisdiction are paid to bill and collect the Education Property Tax. Local jurisdiction keep 0.225 percent of all education property tax collected. In Fiscal Year 2010, this amounted to approximately $2.05 million. The State could redirect this revenue to the Tax Department to fund part of state billing and collection annually, depriving local jurisdictions of this revenue. At stated above, it is unclear whether a drawdown of local actions would occur equal to funds received from the education property tax bills.

Delinquent Tax Collections

The law allows local jurisdictions to designate delinquent tax collectors. These collectors are typically salaried employees of local jurisdictions, though they are not required to be. Delinquent tax collection allows local jurisdictions to keep a statutorily prescribed fee, a percentage of taxes collected. The education property tax is 75 percent of tax billed; therefore, the delinquent tax collector's revenue stream is potentially diminished without the education property tax. Any jurisdiction that counts on delinquent tax fees as part of their budget may see a decline in revenue.

4.3 Impact on Real Estate Stakeholders

State billing and collection would change several important aspects of real estate transactions. Specifically, state billing and collection would change due diligence, tax payment, and escrow functions. These changes to the status quo will likely impose new burdens on professionals involved in real estate transactions and additional costs on taxpayers.

Due Diligence & Tax Payment

Real estate closings require title searches and a clear understanding of taxes owed at the time of closing. Currently, that information is available from local jurisdictions. State billing and collection would require parties involved in real estate transactions to duplicate this effort to determine any State level property tax liabilities owed. This would take more time, and the Tax Department assumes that the cost would be passed onto to the parties at closing. Also, as stated in the previous section, the Department would be required to build into its software system the ability to provide this information to real estate professionals in real time and offer customer service to handle these transactions. Once liabilities are determined, real estate professionals would remit payment to both local and state taxing authorities.

It is important to note that this change may make Vermont an outlier regarding real estate transactions. While a handful of other states have a statewide property tax, Vermont's education property tax is the only substantial, statewide property-based tax in the country. Yet, other statewide property taxes share a common trait with Vermont's current system: billing and collection are done at the local level.[17] Vermont's potential policy choice to create a new property tax payment relationship may create uncertainty for the many real estate parcels that use escrow accounts to satisfy tax obligations through their mortgagee or loan servicer.

State billing and collection of the education property tax would require escrow accounts to pay two separate taxes. Vermont would be unique in this regard, imposing a new obligation on mortgagee's and escrow companies. The impact of changing the traditional relationship between local jurisdictions, property owners, mortgagees, and escrow companies is unclear, given the lack of experience, evidence, and best practices to guide the state in implementation of this change. It is unclear what impact, if any, this change would have on Vermont's real estate market generally and the willingness of national banks, escrow companies, and title companies to do business here.

4.4 Impact on the Tax Department

Responsibility for billing and collection of the education property tax would effect change at the Department of Taxes in three major ways. Specifically, state billing and collection would change departmental technology priorities, potentially change the Tax Department's relationship with taxpayers, and grow the organization.

17 Comparison states include Michigan, Minnesota, New Hampshire, and Washington.

Technology Priorities and Opportunity Costs

The Department of Taxes is undergoing strategic planning for its technology priorities, focusing simultaneously on creating an integrated tax processing system and modernizing our capabilities to serve taxpayers through other one-off projects. The education property tax would insert a new and complex task within that plan. The result would be a lengthening of the VIRCS-ETM project by approximately three years and increasing costs significantly. Also, the Tax Department's ability to complete other technology projects during this time would be diminished as resources flow towards the education property tax project. Any project should be evaluated by both its costs, and issue examined in the preceding section, and these opportunity costs of what projects are delayed or foregone due to new technology priorities. The same principle is true for non-technical projects. The implementation of new priorities can delay other planned and evolving innovation.

Changed Relationship with Taxpayers

The Tax Department will replace local jurisdictions in tasks that taxpayers are accustomed to seeing local jurisdictions perform. Perhaps the most striking example is the sale of homes. Local taxpayers have long accepted that local jurisdictions can sell their home for nonpayment of taxes. Also, it is unknown whether a state tax fueled by a local vote, as this would be, would strengthen the idea that local votes were the primary driver of the rate or whether local voters would further attribute State tax rates and bills to actions taken in Montpelier.

Organizational Change

The Tax Department would likely grow by 20 percent as a result of state billing and collection. This would be in contrast to the past four years of budget and personnel cuts. Also, hiring, on-boarding, training, and retaining these new employees would be a challenge for the organization.

4.5 Impact on the State

The primary impact on the State would be financial. Assumption of state responsibility for billing and collection could impact state revenue in three ways. First, personnel and technology costs driven by the expansion of the Tax Department will draw upon state revenues. This would be offset in part by no longer providing revenue to local jurisdictions for billing and collection of the tax. Instead, these revenues could be budgeted to the Tax Department. Second, state collection of the education property tax may cause the State to carry more delinquencies/billings, and this could impact Vermont's credit rating. Third, the State may be required to make the Education Fund whole for delinquencies. Currently, local jurisdictions are required to remit the tax on behalf of delinquent taxpayers to avoid a shortage in the Education Fund. The State would need to do the same through borrowing or tapping reserves. Alternatively, the State could build a cushion into education tax rates to create a specific delinquency reserve for the Education Fund.

5.0 CLA FORMULAS

5.1 CLA and Current Law

Each year, Vermonters fund education in large part through the education property tax. Fairness requires that every jurisdiction be valued the same way annually. Yet, Vermont's 246 local jurisdictions reappraise properties to their fair market value on a rolling basis over the course of six years. Annual reappraisal of all property in Vermont is impractical and expensive. Accordingly, the State uses the Common Level of Appraisal (CLA) to ensure that all taxpayers pay the education property tax based on their jurisdiction's fair market value.

The CLA affects every education property tax bill in Vermont. The CLA is the ratio of the local assessed values to the State's estimate of fair market value for that municipality. Stated another way, the Tax Department determines how close local grand list property values are to actual fair market values and uses a factor (the CLA) to adjust tax rates to ensure fairness. The mathematical formula is Equalized Tax Rate (ETR) divided by the CLA times the listed value (LV) equals the property tax. Stated mathematically, ETR/CLA*LV = Tax.

While the CLA affects every education property tax bill in Vermont, some argue that it is poorly understood. For example, current law requires the application of the CLA to the tax rate. Therefore, two towns with identical spending per pupil will likely have different tax rates. Also, the application of the CLA to tax rates may give the appearance that the CLA is driving up education property taxes in a local jurisdiction. Such a conclusion reveals a misunderstanding of the CLA's sole role as a tool to ensure that properties are taxed at fair market value annually.

This section of the study will examine the feasibility of "application of the common level of appraisal separately and independently from the tax rate" in accordance with Section 6 of Act 45 of 2011. The application of the CLA is simply an algebraic equation; therefore, it is feasible to enact any of the mathematical variants that will yield the correct tax. The next sub section of the study will introduce four algebraic variants of applying the CLA and describe briefly their potential advantages and disadvantages.

5.2 Four CLA Formulas

Overall, the CLA can be applied in one of three ways. First, the CLA can be applied to and adjust the equalized tax rate (ETR) to ensure that each town's properties reflect fair market value as it does per current law. Second, the CLA can be applied to the listed value (LV) to adjust a particular property to reflect fair market value. Third, the CLA can be applied on its own to adjust the product of the equalized tax rate (ETR) and LV. The study requires the Tax Department to set aside the application of the CLA to tax rates. Therefore, the four variants offered by this study explore CLA applications that either adjust the LV or are applied independently to the product of the ETR and LV.

CLA Variant 1: Fair Market Value Factor

The first variant of the CLA is called *The Fair Market Value Factor*. The CLA would be applied independently to the product of the ETR and LV. Mathematically, the education property tax calculation would be the equalized tax rate times the listed value times the inverse of the CLA: ETR x LV x 1/CLA = tax.

This application has the potential to create some additional clarity as the first two steps of the calculation mirror most property taxes. Specifically, steps one and two of the calculation are tax rate times listed value. Next, the formula adjusts the amount due to account for fair market value. This highlights that the CLA is not driving up tax rates. For example, towns with the same per pupil spending will have the same tax rate despite variations in assessments. Also, local listed values are left alone. Yet, this additional clarity comes with the potential for confusion as well. The Fair Market Value Factor adds a third step to the property tax calculation, currently it is a two step calculation, and explaining the use of the inverse of the CLA may be challenging and confusing.

CLA Variant 2: Fair Market Value Factor Two-Step

Variant 2 builds upon Variant 1. Specifically, the Fair Market Value Factor Two-Step divides the formula into two steps to reduce the potential confusion. Mathematically, the variant would work as set forth below:

- Step 1
  - ETR x LV = municipal value tax
- Step 2
  - Municipal value tax x 1/CLA = fair market value tax

Each taxpayer is assessed (or gets a reduction) to the tax amount, each at the same rate, to adjust for the variance between the town's education grand list and the State's equalized education grand list. In the case where a town's education grand list is less than the equalized education grand list, each taxpayer pays a prorated assessment in step 2 to make up the shortfall. Conversely, in the case where a town's education grand list is more than the equalized education grand list, each taxpayer pays a diminished assessment in step 2 to prevent overpayment.

Like the first variant, this formula has the potential to clarify the CLA by separating it from tax rates. Also, local listed values are left alone. Yet, two issues of potential confusion are added. First, there is a potential for taxpayers to confuse the municipal value tax with the traditional municipal tax. Second, there is a risk that some taxpayers may perceive that Step 1 is what taxpayers would pay but for State intervention. Step 2 is either a premium or discount offered by the State. Of course, the CLA only adjusts the tax to account for variations in the appraisal to fair market value. The State is not choosing by policy or fiat to use the CLA to drive taxes up or down.

CLA Variant 3: Direct Equalization

Rather than adjusting the tax rate or applying the CLA independently, the State could apply the CLA to listed values directly. This direct equalization would adjust each property value to reflect fair market value for education property tax purposes. Mathematically, the education property tax calculation under Direct Equalization would be the listed value divided by the CLA times the tax rate: LV/CLA x ETR = tax.

Direct Equalization has two major benefits. First, local jurisdictions with the same per pupil spending levels would have the same tax rates thus making the funding system more understandable. Also, the formula would incent property owners with listed value assessments significantly different from the town's average level of appraisal (i.e., the CLA) to appeal their valuation to attain a more equitable level of valuation.

Direct Equalization has two major drawbacks. First, the formula presents significant problems for local jurisdictions as to whether there is any due process requirements for appeal of "equalized" valuations used to set tax amounts. If there was, it would mean that either the towns or the State would have to provide a second lengthy due process system. Second, because the CLA is a town wide "average" and individual listed values typically vary significantly above and below it, the resulting taxable values would tend to vary considerably from the town's established listed values.

CLA Variant 4: Setting Local Liabilities

Alternatively, the State could return to the mechanism employed under Act 60 and modified by Act 68. In this variant, the State would set a liability for each town using a state "equalized" tax rate and the state's estimated equalized property value and then require towns to set a local tax rate sufficient to raise the required liability.

6.0 PUBLIC COMMENT

6.1 Public Comment and Future Appendices

The Tax Department is interested in stakeholder comments on the feasibility study. Accordingly, Tax Department staff will distribute the feasibility study to key stakeholders and solicit feedback. The Department will compile the options and issues identified by stakeholders and append a summary of stakeholder comments. This supplemental work will be completed prior to the 2012 legislative session.