

Vermont's Tax Structure

Total Revenue and State Revenue, FY2015



Prepared for the Vermont Democratic Caucus

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Vermont taxes are relatively progressive

Most Vermonters pay all 3 major taxes (income, consumption, and property taxes) and see interplay among them and with the federal tax system

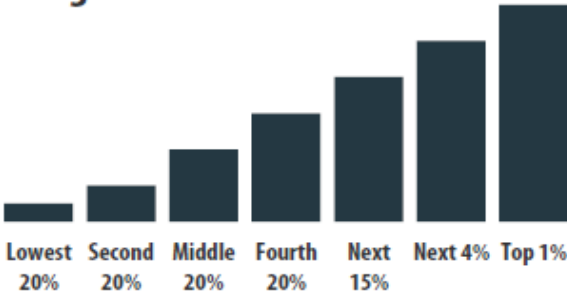
- Vermont's income tax structure is progressive
 - JFO case studies from The Vermont Tax Study using 2015 data demonstrate progressivity
 - We analyzed state taxes as a share of household income
 - Vermont is the 10th lowest tax state for low-income households
 - Vermont is in the middle of states for taxes as a share of income for middle-income households
 - Vermont has the 10th highest taxes as a share of income for high-income households
 - Progressive income tax structure results in low effective tax rates for most taxpayers: 3.2 percent on average in 2014
- Consumption taxes such as sales taxes or gasoline taxes are regressive but Vermont softens this by exempting food and clothing
- Property tax structure is flat because some homestead property taxes are based on income

How does our tax system compare to that in other states?

- Institute on Taxation and Economic Policy (ITEP), “Who Pays?” 2015
 - Emphasis on progressivity: Examine distribution of state and local taxes by income groups for nonelderly taxpayers
 - Vermont ranked 46 out of 50 states, meaning that only 4 states had a more “fair” tax structure
- Tax Foundation Business Climate rankings, 2018
 - Emphasis on low rates, simplicity, neutrality (not affecting business decisions)
 - Vermont ranked 47 out of 50 states, meaning that only 3 states had a worse tax structure for business climate

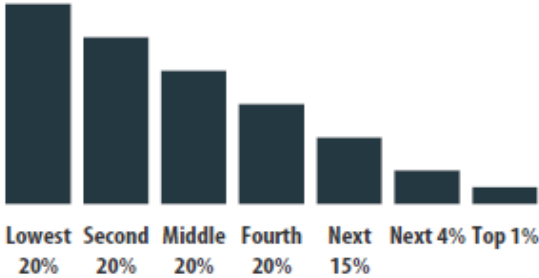
What does tax fairness/progressivity mean?

A Progressive Tax



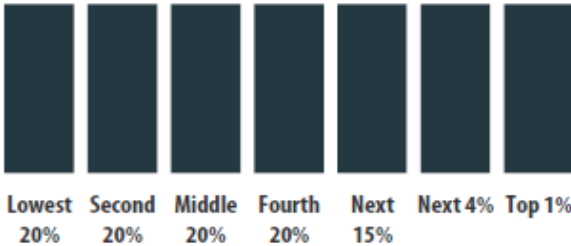
A **progressive tax** is one in which upper-income families pay a larger share of their incomes in tax than do those with lower incomes.

A Regressive Tax



A **regressive tax** requires the poor and middle-income to pay a larger share of their incomes in taxes than the rich.

A Proportional Tax



A **proportional tax** takes the same percentage of income from everyone, regardless of how much or how little they earn.

Progressive income tax structure results in low effective tax rates for most taxpayers

- Tax rates rise with income: progressive

- On average, VT’s effective tax rate is 3.2%

- ~370,000 VT income tax returns in TY 2015

- 86% or ~318,000 from resident taxpayers

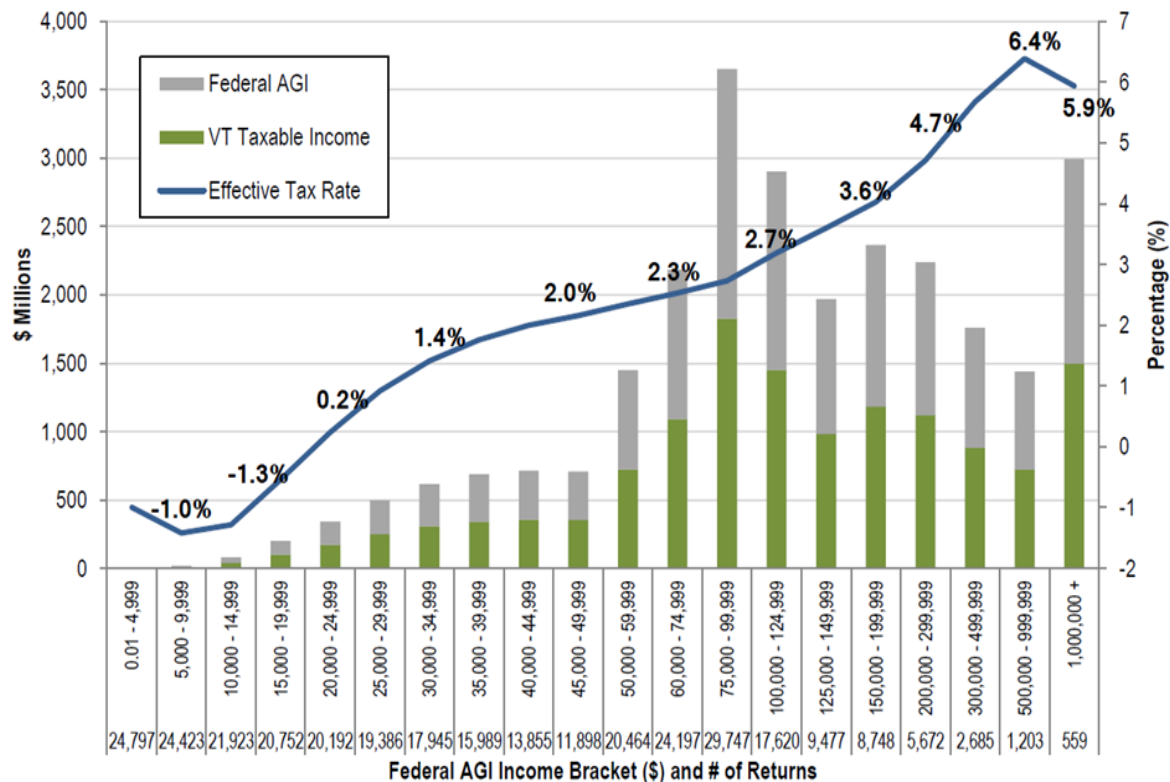
- Based on taxable income

- = AGI

- personal exemptions

- (standard deduction OR itemized deductions)

Figure 14. Effective Tax Rates and VT Taxable Income as a Share of Federal AGI, Tax Year 2014



The top 10% of resident filers paid 61.5% of individual income tax revenue in TY 2015

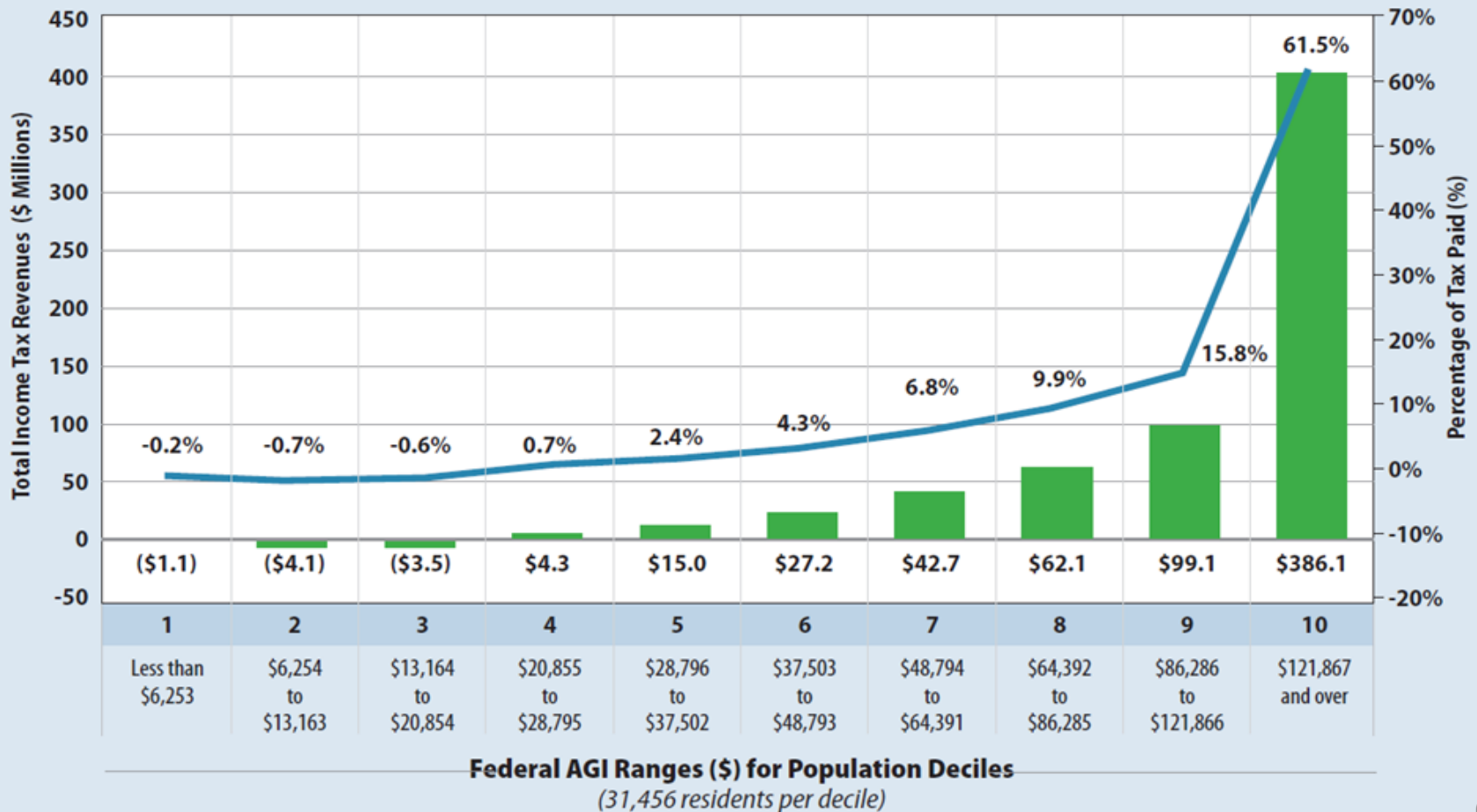
top 10% of tax filers have federal AGI > ~\$122,000

The top 5% of resident filers paid 48% of individual income tax revenue in TY 2015

top 5% of tax filers have federal AGI > ~\$155,000

Shares of Vermont Income Taxes Paid by Each of 10 Income Groups (Deciles)

Tax Year 2015



Consumption taxes are regressive for many Vermonters

- Types of consumption taxes in Vermont
 - Sales and Use tax is 6% on tangible personal property
 - Communities may exercise a 1% local option sales tax
 - Exempted to avoid tax pyramiding: inputs for manufacturing
 - Exempted businesses: nonprofits and agricultural entities, farming products
 - Exempted to avoid regressive taxes: groceries, OTC medicine, clothing and footwear
 - Meals and Rooms tax
 - Taxes on cigarettes, alcohol, motor fuel
 - Other consumption taxes
 - Health care taxes paid by health care providers, commercial insurance companies, and consumers
 - Fuel tax paid by retailers
- Why are consumption taxes regressive?
 - Young and/or lower-income households spend a greater share of income on items that are taxed
 - Food away from home, cigarettes and alcohol, vehicles and fuel
 - Older households spend more on health care and housing

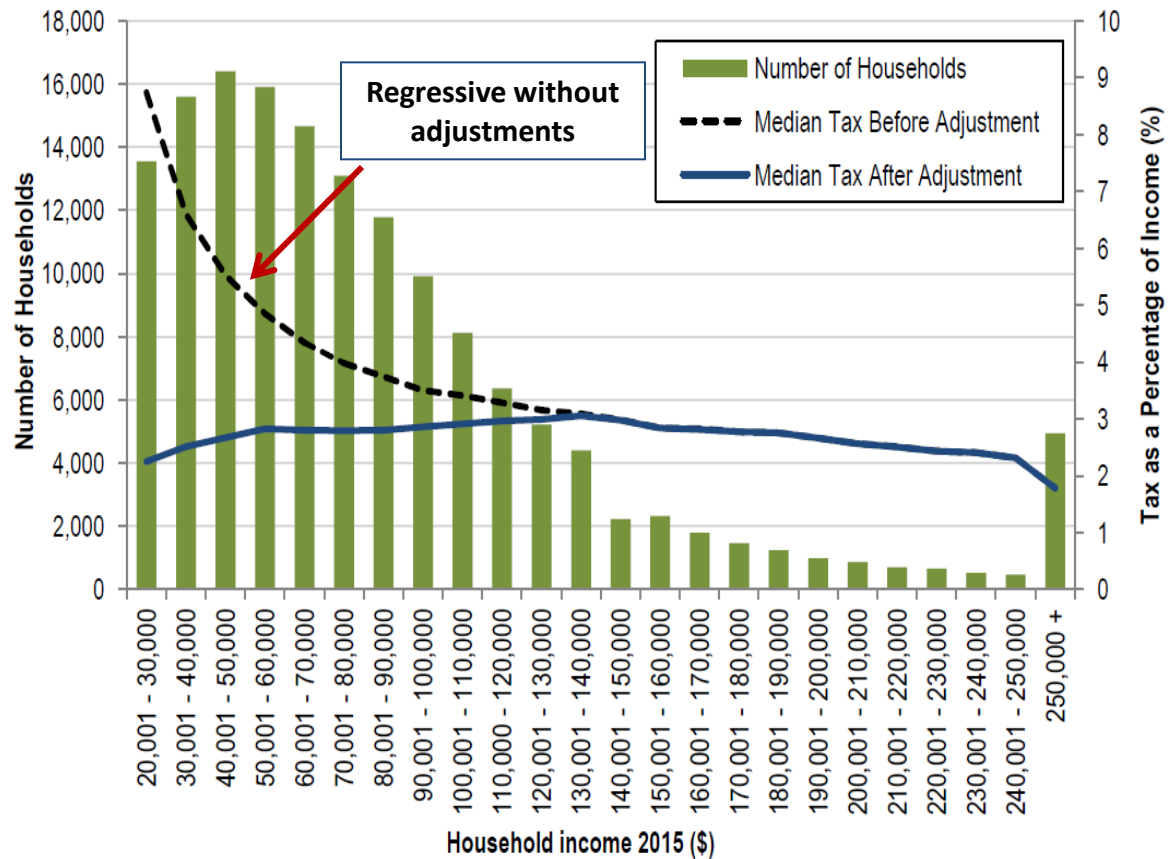
The property tax in Vermont is flat...

- Vermont's statewide education property tax is unique and consists of two parts
- Homestead education tax on a primary residence and contiguous land (41% of property tax revenue received)
 - Statewide tax rate is adjusted in each community based on local education spending per pupil, then further adjusted to equalize property tax obligation statewide
- Nonresidential education tax on second homes and rental, commercial, and industrial properties (59% of property tax revenue received)

...but would be regressive without income sensitivity for homestead taxes

- In FY 2015, 66% of homestead parcels or 110,358 households got some type of property tax adjustment
 - Applies only to tax due on house + 2 adjoining acres
 - Capped on property taxes > \$8,000
 - If household income < \$90,000, portion of tax subject to income sensitivity is limited to tax due on first \$500,000 of house site value
 - Partial benefit if household income is between \$90,000 and \$108,889
- Overall, 14% of total education property tax revenue was based on household income, the remaining 86% on the fair market value of property

Figure 39. Education Tax as a Percentage of Household Income, CY 2015



For additional information

The Vermont Tax Study, 2005-2015

- Summary Report
 - <http://www.leg.state.vt.us/jfo/reports/2017%20VT%20Tax%20Study%20Summary%201-17-2017.pdf>
- Full Report
 - <http://www.leg.state.vt.us/jfo/reports/2017%2010%20Year%20Tax%20Study%20Full%20Report%20Compressed.pdf>

For historical perspective, see

Final Report: Blue Ribbon Tax Structure Commission, 2011

- <http://www.leg.state.vt.us/jfo/reports/2011%20Blue%20Ribbon%20Tax%20Structure%20Commission%20FINAL%20REPORT.pdf>

How might Federal Tax Reform affect Vermont's tax system?

- Vermont is linked to the Federal tax system in many direct and indirect ways. Some major examples include:
- Changes to Adjusted Gross Income (AGI):
 - Could affect eligibility for several Vermont programs and tax credits.
 - Repealing some deductions could raise AGI and increase Vermont Taxable Income (VTI), income subject to Vermont tax rates.
- Changes in deductions:
 - Repealing or limiting itemized deductions could increase or decrease VTI.
 - Increasing the size of the Federal Standard Deduction could increase or decrease VTI
- Any change to Federally-linked tax credits could affect the size of a related Vermont tax credit.

Other Key Points

- **Situation is currently in flux and complicated.**
 - Bills are not finalized.
 - Many indirect impacts/behavioral responses are possible.
- Federal tax reform will affect a Vermonter's federal and Vermont tax liability.
- Other impacts could be broad:
 - In the long term, these changes will likely impact Vermont's economy as a whole as businesses and individuals adjust to the changes at the federal level.
 - Corporate tax reform will have additional effects as corporations respond to federal rate changes, affecting the state's economy and state revenues.
 - Reduced federal revenues could have impacts on the availability of funds for state grants and federal benefits to individuals.