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Policy Primer: Reforming Our Property Tax System

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The less money you make in Connecticut, the higher the share of that income you pay in local property taxes. This is true across the nation, with Connecticut's disparity among the widest. And disparities also are great from town to town in Connecticut because municipalities in the state rely heavily on property taxes to pay for education and critical services, such as police and fire protection, and have large differences in home values.

As a result, communities can't offer children an equal shot at opportunity when local educational resources vary widely, and families are burdened by high housing costs and the state's unfair property tax system.

Connecticut households with an annual income around $20,000 pay 12.5 percent of their income in property taxes. In contrast households with an average income of around $42 million pay just 0.92 percent, according to a report by the Connecticut Department of Revenue Services.[1]

A report by the Federal Reserve illustrated wide disparities across municipalities, finding that the wealthiest towns have an average per capita revenue capacity – defined as resources that local governments are authorized to tax – nearly eight times more than urban communities.[2] These disparities mean that the property tax rate (also called "mill rate") varies sharply by town in order to raise sufficient revenue, ranging from $10.70 per $1,000 of taxable property in Salisbury to $74.29 in Hartford.[3]

Connecticut's State Tax Panel agrees that that the property tax system is in need of reform. After an extensive review of all state and local taxes, the State Tax Panel issued a report at the end of 2015 that made several recommendations. The recommendations included the implementation of a "circuit breaker" that would limit property taxes to a certain proportion of income; strengthening the underfunded state program that compensates municipalities for revenue lost because of facilities that don't pay property taxes (like govern buildings and colleges); and examining state grant policies to equalize fiscal disparities among Connecticut's municipalities.[4]

The Panel's discussion often shifted towards whether or not wealthy and elderly citizens are leaving Connecticut to avoid estate and income taxes, with expert testimony to the Panel finding no evidence of significant numbers of people leaving because of taxes.[5] Instead, research shows that housing costs, family and job considerations, and climate are much more likely than taxes to prompt a state-to-state move.[6] According to IRS data, 26-to 34-year- old and low-income taxpayers are most likely to leave Connecticut.[7]

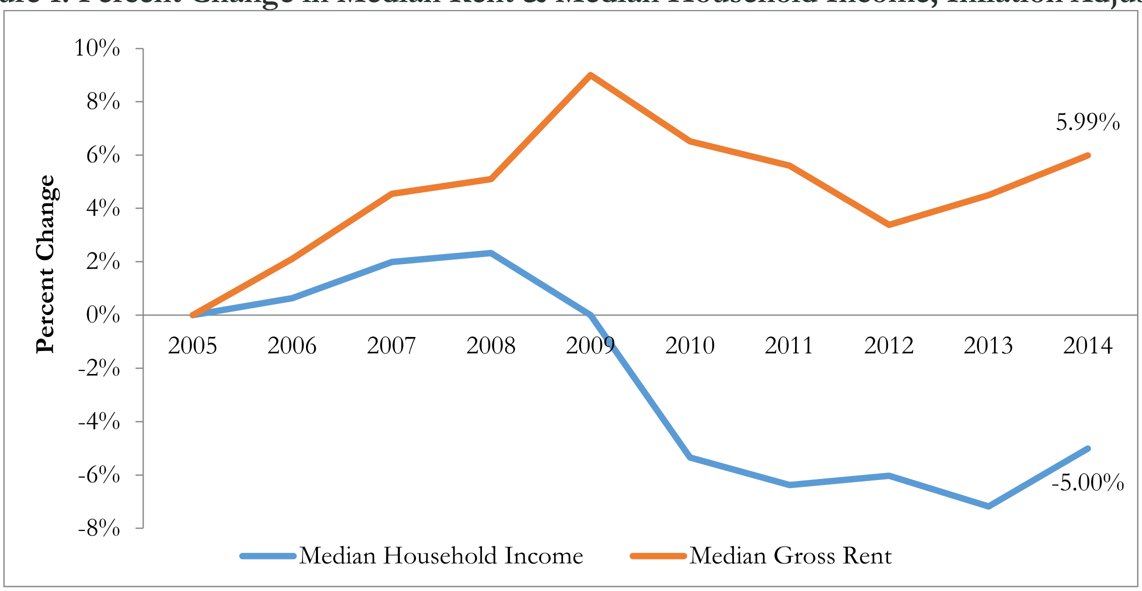
Testimony to the Panel made clear that "high property tax rates, if not balanced by high service levels, discourage families and businesses from locating or expanding in a jurisdiction", and empirical work found that reducing property tax rates will encourage economic growth (while education *spending* was found to stimulate growth).[8]

Therefore, property tax reform is not only an opportunity to reduce the enormous gaps among towns, and help all children in all places get an equal opportunity to succeed, but also to encourage economic growth and to retain families who, in the wake of a low-wage economic recovery, have seen housing costs escalate. The following policy changes would help reach these goals:

Create a Low-Income Circuit Breaker: To promote tax equity, current property exemptions should be reformed to target relief based on income, freeing up resources for a family's basic necessities such as childcare, transportation, and food. A refundable property tax circuit-breaker does just that -- similar to how an electric circuit breaker stops the flow of current to prevent a circuit overload. The property tax circuit breaker reduces the tax liability, via a rebate, when property tax payments reach a certain percentage of family income. Over 34 percent of Connecticut homeowners now pay more than 30 percent of their income on housing.[9] According to research presented to the State Tax Panel, Connecticut ranks second in per capita property taxes ($2,626), nearly double the U.S. average ($1,421).[10]

Renters – whose costs increase with high property taxes passed on to them by landlords as part of the rent – would also receive the refundable credit. Among states, Connecticut has the sixth largest share of residents whose rent amounts to more than half their income (28.5 percent). And the state has the 16th largest share of residents that pay between a third and half of their income in rent (23.2 percent).[11] As incomes stagnate or decline, while the cost of rent increases, more and more families are paying a higher percentage of their income on rent and less on other basic necessities (*Figure 1*).

Figure 1: Percent Change in Median Rent & Median Household Income, Inflation Adjusted



Source: CT Voices analysis of American Community Survey data

Enact a Statewide Property Tax: Disparity among towns' capacity to raise revenue results in huge gaps in school spending between different communities. Per-pupil spending ranges from $12,444 in Woodstock to $30,342 in Cornwall – a difference of $17,898 per student.[12]

One way to ensure equitable opportunity for all students is to create a statewide property tax system. Presented as a "discussion document" to the Panel, and not included in its recommendations, the proposal calls for the share of local property tax revenue now used to fund education (approximately 60%) to be collected by the state instead of municipalities, and distributed in a way that equalizes school funding.

Property taxes in towns with low- to moderate incomes would go down an average of $207; residents of the wealthiest communities would see an average increase of $597.[13]

Re-structure state grant policies to relieve pressure on the property tax and to reduce fiscal disparities: Although members of the State Tax Panel thought that addressing the magnitude and design of state grants to local governments was beyond the scope of its work, the Panel did observe that there was evidence of significant differences in property tax capacity of municipalities, as noted above. So the Panel recommended that further study be undertaken. One possible option is set out below:

> **Strengthen Payments in Lieu of Taxes (PILOT):** Non-school PILOT grants from the state attempt to alleviate fiscal inequities by compensating municipalities for property tax revenues lost due to state-owned, tax-exempt property, private universities and nonprofit hospitals being exempt from local property taxes. While nonprofits do provide a pubic good, tax exemptions are criticized for being poorly targeted and for the "geographic mismatch" they create, in which costs they impose are borne locally (roads, fire, and police, for example, while the benefits often expand beyond borders.[14]
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> The PILOT grants have long been underfunded, currently leaving 75 percent of total liability not covered, while municipalities collectively lose more than $500 million per year in foregone revenue.[15] Of those, Hartford and New Haven make up the two biggest losers, collectively losing more than $170 million annually. They also are among the state's poorest and most economically segregated cities.[16] The panel recommended retaining the existing statutory PILOT programs, although it made no recommendations for funding them. It also observed that under existing law, municipalities can develop voluntary PILOT programs, such as those based on the "Boston Model", in which "exempt organizations contribute to the cost of publicly provided goods and services (such as police and fire protection and public works, such as street cleaning and snow removal) that benefit the organization."[17]

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